

FINANCIAL TIMES

BRUSSELS
Struggle to remove takeover barriers
Page 5

No.31,009 Monday November 27 1989 D 8523A

World News

Congress set to lose seats in Indian assembly

Prime Minister Rajiv Gandhi's Congress Party appeared to be heading for defeat last night in a general election likely to herald a period of political instability in India. Early trends in the counting suggested that the Congress party would win about 200 of the 525 contested seats, compared with the 416 it won in 1984.

Hrwai challenge

Elias Hrawi, Lebanon's new president, said he will use force if necessary to break General Michel Aoun's hold on the Christian enclave. Gen Aoun vowed not to submit without a fight.

Salvador breaks ties

El Salvador suspended diplomatic and commercial relations with Nicaragua following the discovery of an arms shipment of 24 surface-to-air missiles on a light aircraft which allegedly came from Nicaragua.

W Bank arrests

Israeli troops lifted curfews on more than 14,000 Arabs in the occupied West Bank after making scores of arrests, residents and the army said.

Uruguayans vote

Uruguayans voted in their first free elections for 16 years, with some casting their ballots for one-time guerrillas, political prisoners and others who suffered under more than a decade of repression by the armed forces.

Poles burn cards

Some 200 young Poles protesting against conscription marched across Warsaw towards the presidential palace and some publicly burnt their army identity cards. Soviet visit.

Yemen unity 'closer'

North and South Yemen have narrowed differences on unification and are pressing ahead to reach agreement on the South Yemen's Minister for Unity Affairs Rashid Mohammed Thabit said.

Cambodia fighting

Cambodian guerrillas of the Khmer People's National Liberation Front breached government positions on the outskirts of a strategic north-western town near the Thai border and claimed to hold 70 per cent of the town of Svay Chak.

Roh visits UK

President Roh Tae Woo of South Korea arrives in Britain today for an official visit which will concentrate on trade and business issues, with Korean barriers to British whisky imports certain to be raised.

Yes for Swiss army

Swiss voters rejected by a majority of less than 2-1 a draft law to abolish the country's militia army by the year 2000, in a referendum without precedent worldwide.

Ukrainians march

More than 150,000 people carrying portraits of Pope John Paul marched through the west Ukrainian city of Lvov demanding the legalisation of the Ukrainian Catholic Church.

ANC rally

Two people were killed and several injured in the black homeland of Transkei when tear gas and gunshots were fired at a church rally welcoming four African National Congress leaders.

Kvant-2 problems

A Soviet module heading for the orbiting space station Mir developed difficulties with one of its solar batteries, Tass news agency said. The Kvant-2 module developed a problem after separating from the Proton rocket which launched it yesterday.

US sumo victory

Hawaiian-born sumo wrestler Kozishiki became the second foreign wrestler to win a major Japanese tournament when he forced his Japanese opponent out of the ring. Page 3

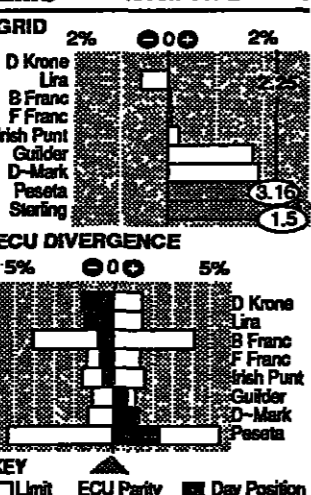
Business Summary

Grenfell tries to fend off takeover with bank deal

MORGAN Grenfell, London merchant banking group, is expected to announce today that it has struck a deal with Deutsche Bank, after a week-end of last-ditch negotiations to fend off a likely takeover bid from Banque Indosuez, French bank. Page 6

EUROPEAN Monetary System: Demand for the D-Mark - the dollar fell below DM1.80 for the first time since January, at one stage on Friday - renewed speculation about an early EMS realignment. The lira was the weakest EMS member, but is allowed a wider cross rate limit than most other currencies and was not under any immediate pressure. The French franc was weak, but did not appear to suffer from suggestions that remaining French currency controls will be scrapped next month. Currencies, Page 38

EMS November 24 1989



The chart shows the two constraints on European Monetary System rates.

The upper grid, based on the weakest currency in the system, defines the cross-rates from which no currency (except the lira) may move more than 2 1/2 per cent. The lower chart gives each currency's divergence from the 'central rate' based on the least currency in the system, a basket of European currencies. Calculations based on Monday-Thursday data. Friday data not available.

GENERAL Motors has begun supplying engines from South Korea to its operations in West Europe for the first time, in order to alleviate production bottlenecks and lack of capacity at its European engine plants.

THE OECD has called on the US to carry out radical changes in its tax system to remove impediments to saving. Page 3

DEFENCE: The British Government is making urgent efforts to arrange a bank loan of around £2bn (\$3.15bn) to finance continued Saudi Arabian purchases of military equipment under the UK's huge Al-Yamamah defence contract.

ENIMONT, Italian public-private chemicals joint venture, looks set for a starring role on the Milan stock exchange because of serious doubts about whether Mr Raul Gardini's Montedison ultimately intends to hand on to its 40 per cent stake. Page 25

OIL: Pressure is building in Norway, Western Europe's second largest oil producer after Britain, to abandon a 7.5 per cent curb on crude oil production.

CAMFIL, a privately owned Swedish filtration company, is to buy Sofitra-Poelman, industrial filters subsidiary of the leading French glass and pipes group Saint Gobain. Page 25

IBCA, London-based rating agency specialising in bank credit analysis, promoted five Japanese banks to its top-rated AAA category bringing to 13 the number of international banks given its highest rating; Japanese banks were previously absent. Page 25

AUSTRALIA: The Government unveiled details of its first reverse bond tender to retire federal government domestic debt, confirming its continuing withdrawal as a borrower and forcing a significant adjustment on the country's capital markets. Page 25

JAPANESE banks' profits have been squeezed by rising interest rates, forcing some of them to announce their first reductions in interim net profits since 1981, the year they started reporting interim figures. Page 25

A million protesters march as Czech premier meets Civic Forum opposition group

Adamec opens direct talks

By John Lloyd in Prague

MR LADISLAV ADAMEC, Czechoslovakia's Prime Minister, yesterday threw aside the grudging response of the country's Communist Party to the demand for political reform and entered into direct negotiations with the opposition movement, Civic Forum.

As the historic talks got under way up to one million people marched in cities across the country calling for democracy. The dispirited Communist party's decision-making central committee later began an evening crisis session, its second in three days.

Mr Adamec, along with two senior party officials, held talks with a nine-member delegation from Civic Forum, headed by Mr Vaclav Havel, the dissident playwright.

Yesterday's talks, which lasted an hour, marked the first occasion on which the country's opposition movement has forced the government into negotiations. Both sides agreed to meet again tomorrow.

The nine opposition delegates presented the Prime Minister with demands which they say should be met by then.

These include the release of all political prisoners - about 50 on the opposition's count - an end to censorship and an independent inquiry into security force violence against peaceful demonstrators on November 17.

The dialogue with the opposition followed the decision of Mr Karel Urbanek, the new Party leader, to break with the

refusal of his predecessor, Mr Milos Jakes, to talk with critics. "We have become isolated from the people and the truth," Mr Urbanek said on Saturday, one day after replacing Mr Jakes, who resigned along with the entire Party secretariat, or top leadership, on Friday evening.

Later yesterday, Mr Adamec, who quit his Politburo and government posts last Friday but is staying on as caretaker head of government, told a flag-waving crowd of 400,000 demonstrators on Prague's snow-swept Letna parade ground that the Forum's demands would be relayed to the party central committee, which met in a second crisis session last night.

Mr Adamec called for national unity and the participation of all peoples of good will but was booed and whistled when he called for calm and suggested that the two hour strike called for today might be cut to two minutes. Mr Adamec said: "There is no time for disagreement and fights for prestige...people will judge us by our ability to overcome the past."

His appearance on the rostrum was followed by one from Mr Alexander Dubcek, the former Communist Party leader deposed by the Warsaw Pact invasion in 1968, who gave his most powerful speech yet. He demanded that the Czechoslovak party - and with it the Soviets, East Germans and Bulgarian party leadership -



Czech opposition leader Vaclav Havel (left) shakes hands with Prime Minister Ladislav Adamec at the start of their talks in Prague yesterday

politise for the invasion. Mr Dubcek, who is now regarded by many as a serious candidate for the Presidency, directly contradicted Mr Adamec's call for calm. Addressing the largely youthful crowd, he said: "Twenty one years ago your fathers and mothers were fighting, and now you are fighting. Thank you for your initiative and your fathers and mothers are with you."

Mr Vaclav Havel, the Civic Forum leader, said that the opposition had called for popular support for Mr Adamec, on the grounds that he was waging a battle with party hardliners. Nevertheless the Prime Minister was met with cries of "resign" by many in the crowd. Over 700 factories and enterprises have voted to support an opposition call for the strike. Mr Havel has described the action as a referendum on the party's power monopoly.

Mr Karel Urbanek the new

Czech spirit blooms in the Prague winter

By Judy Dempsey in Prague

THEY CAME from south Moravia and north Bohemia, from Kosice and Bratislava to join in this massive reawakening of the Czech spirit which, after 21 years of silence, burst out in full bloom on Letnska Plain, a vast space not far from Hradcany Castle.

While the Communist Party elite moved out of the Castle, once the home of the kings of Bohemia, to hold its emergency central committee session in the Party school, the crowds began to take power into their own hands.

In bitterly cold temperatures of minus 5 centigrade, they heard people, who were once muted by the new regime, now speak the language of freedom and truth.

On Saturday afternoon, Mr Vaclav Havel, the once shy and modest playwright,

received a tumultuous welcome which resounded throughout Prague. "Na Hrade," - to the Castle, they roared.

Mr Alexander Dubcek, who spearheaded the Prague Spring of 1968, who joined the podium on Saturday, received the same compliments. For the people, both men are deemed fit citizens to take over the mantle of leadership.

Many of the half a million people, coloured by a sea of Czechoslovak red, white and blue flags, wound their way down from Letnska Plain to the old city and again convened in the square.

By the early hours of yesterday, the square was a veritable information centre. Young students, armed with independent newspapers hot off the printing presses, gave them

EASTERN EUROPE

- No confidence in Krenz
Excuses run out
Obstas of Katyn
Weisskoffer 'proposal'
All together, now

away freely to taxi drivers and anyone walking up this majestic boulevard. Even at 2am, the younger generation of Czechoslovaks were eager for more action.

Shops are now plastered with posters, slogans and notices. Demonstrations, some calling for a general strike, others calling for free elections. But most of them proudly display one name: Obcanske Forum - the Civic

Forum, which, with remarkable speed and organisation, has brought together all the disparate elements of the opposition.

Its headquarters are located in the basement of the Magic Lantern Theatre, just off Wenceslas Square. There, while the cohorts of the Civic Forum spend hours locked away in consultations over their next move and how they should talk to Mr Ladislav Adamec, the Prime Minister, Mr Jan Urban, head of Obruda, a banned organisation for those party members who have been expelled by the country's former party chief, Mr Milos Jakes, remained on the ground floor of the theatre.

It is he who picked the timetable of press conferences, briefings, circulars and information flowing freely as if he

was trained in public relations.

Crowds gather outside to catch the latest news about what the Civic Forum is doing. A television, perched on a window sill, broadcasts regular bulletins throughout the day. The people are excited. Students flock in to help type statements or distribute them. Everyone has become a politician or a campaigner.

Just like the staff in many of the hotels along Wenceslas Square who have the radio and television on all day and who are now taking politics into their own homes.

The local party branch in the Jalta Hotel has a trite notice displayed on its front door, disowning the party's brutal attack on the young student demonstrators on the Continued on Page 20

Airbus finance chief set to quit

By Paul Betts, Aerospace Correspondent, in London

AIRBUS INDUSTRIE'S top management seems set to be thrown into turmoil with the imminent resignation of Mr Robert Smith, who was recently appointed the group's finance director as part of an overhaul of its management.

The likely resignation coincides with the launch yesterday of the \$480m research and development programme for Airbus' new A-321 aircraft.

The four nation European aircraft manufacturer will fund the programme by selling the consortium's financial markets for the first time, rather than relying on traditional government support.

Airbus is close to finalising details of the package with a group of banks. The move highlights the consortium's efforts to adopt a more commercial approach.

Airbus officials confirmed yesterday the formal launch of the new A-321 short to medium range 186 seat aircraft, a stretched derivative of its best selling 150 seat A-320, but declined to comment on the expected resignation of the British finance director.

Mr Smith was succeeded from

British Aerospace's Royal Ordnance subsidiary seven months ago to take over the post of Airbus finance director which was specially created as part of a broad overhaul of the consortium's management structure earlier this year.

The likely resignation coincides with the streamlining of the consortium's top management, was designed to help cut costs and give Airbus a more business-like and market-oriented management structure.

However, Mr Smith appears to have grown increasingly disenchanted over the difficulties of improving the efficiency of the consortium's financial structures and he is understood to have decided to resign. He is not expected to return to BAe.

He would become the second BAe executive to leave Airbus in recent weeks. Mr Adam Brown, the former vice-president in charge of strategy at Airbus, left the consortium last month after criticising BAe's attitude towards the four nation aircraft manufacturing group.

The four partners in the Airbus consortium include Aeros-

patiale de France (37.9 per cent), Messerschmitt-Bölkow-Blohm of West Germany (37.9 per cent), BAe (30 per cent) and Casa of Spain (4.2 per cent).

The top management strains at Airbus come at a time when the European consortium is enjoying record orders and is seeking to convert its commercial breakthrough in the world civil aircraft market into financial success.

But the consortium has continued to be shaken by a series of disputes between its partners and the nationalistic rivalries of their respective governments.

This has included a major row over West German demands, fiercely opposed by France, for the transfer of the final assembly of the A-320 from Toulouse in south-west France to Germany.

Further clouding the horizon for Airbus is continuing uncertainty over the intentions of Mr Jean Pierson, the consortium's chief executive and one of the principal architects of the recent commercial successes of the group, to seek a Continued on Page 20 Details, Page 8

CONTENTS THE MONDAY INTERVIEW



Mr Li Ka-shing, who runs a Hong Kong business empire worth over \$3bn, faces the dilemma of whether to move his group's domicile out of the colony, thus keeping international investors but damaging local business confidence. Page 42

Table listing various market news items and their corresponding page numbers, including sections for Czechoslovakia, Management, Editorial comment, US Savings and loan scandal, Economic viewpoints, Surveys, Business columns, Letters, Stock Markets, Wall Street, London, UK Gilt, UK Gilts, Unit Trusts, and Weather.

## INDIAN ELECTIONS

## Constitution poses problems for President

By K.K. Sharma in New Delhi

THE Indian Presidency has rarely been in a position where it has been forced to play a political role. Like the British monarchy on which it is based, the office has mostly ceremonial functions.

This week, however, 78-year-old Mr. Ramaswami Venkataraman, the present incumbent, will be called on to make decisions that will not only determine which party or combination of parties will form the next Government, but will also set constitutional precedents.

Mild-mannered, soft-spoken and retiring, Mr. Venkataraman has had a distinguished and non-controversial political career. He is widely expected to act independently this week when he performs his constitutional duties.

Mr. Venkataraman intervened firmly last week when he asked the Election Commission to inquire into complaints about unfair election practices at Amethi, where Prime Minister Rajiv Gandhi contested the election. Opposition members who met the President with their complaints quoted him as saying that democracy and violence cannot go together.

Mr. Venkataraman has been

the powers of the President and says merely that he should invite the leader of a party who commands majority support in the Lok Sabha (lower house of Parliament) to form the Government.

Mr. Venkataraman faces crucial decisions over three issues. The first is, who should be called to form the new Government. Second, whether he should dissolve the previous Lok Sabha whose term lasts till January 14, 1990. Third, what should be done about checking "defections", or members switching parties after being elected.

Mr. Venkataraman has been urged not to act on the advice of Mr. Gandhi, whose ruling Congress Party still has a majority in the existing Lok Sabha. Constitutional experts have reacted with horror to the possibility of Mr. Gandhi continuing in power when he has clearly lost his mandate. In deciding on who should form the next Government, the President can call on Mr. Gandhi as leader of the largest single party. This is in line with the constitutional practice of letting the largest party have first try.

Alternatively, he can decide to call on the leader of the Janata Dal as the largest group opposing Congress. This would be in keeping with the practice of allowing the Opposition to



Voting counting in New Delhi is disrupted by disputes over the validity of ballot papers

form the Government when the ruling party has no chance of doing so.

Taking the realities of the situation into account, the President seems most likely to call the leader of the National Front, Mr. V.P. Singh, as the leader best placed to form an administration with a majority in the Lok Sabha. Mr. Venkataraman really has no Indian precedent to guide him except for the events that followed the resignation of Mr. Morarji Desai as Prime Minister in 1979 when the Janata combine cracked up.

The then President, Mr. N. Sanjiva Reddy, first called Mr. Y.B. Chavan, leader of the (Congress) Opposition to try to form the Government. When Mr. Chavan failed, Mr. Reddy

asked Mr. Charan Singh, leader of a Janata breakaway group supported by the Congress, to be Prime Minister. Mr. Charan Singh resigned a few months later when Congress withdrew its support.

The only authoritative advice available to the President is that given by Mr. Justice Sarkaria in a report on centre/state relations. Mr. Sarkaria says, in speaking about selecting a chief minister in a state where there is no clear majority, that the governor should invite a leader of an alliance of parties formed before an election, if the alliance is the largest party.

Mr. Venkataraman is believed to have been studying all such precedents in Britain and

India in preparation for his task this week.

Mr. Nani Palkhivala, the noted constitutional lawyer, says whatever the President does will "become an established precedent, for good or evil, which would probably be followed when a similar situation arises hereafter".

Mr. Palkhivala says: "The President has to ensure that a 'hung' Parliament does not result in public morality being hanged. Few people realise that a high moral tone is of the essence in the Indian constitution. The President has to make such a value-based decision that democracy may survive in India beyond our own times".

## Leaders must overcome bitterness and mistrust

By David Housego in New Delhi

AS India's opposition leaders last night began to face up to the prospect of forming an administration, it was clear that the difficulties will be as great as any they had imagined.

After the violence that marked the polling and the allegations of rigging in Prime Minister Rajiv Gandhi's own constituency of Amethi, it was also clear that cabinet making would take place in an atmosphere of bitterness and mistrust.

Opposition supporters are likely to take to the streets if they feel that Mr. Gandhi's Congress party - or the President - are attempting to deprive them of the right they feel they have won at the ballot box.

Congress, on the basis of early returns, will have about 200 of the 525 seats contested in the new Assembly and will therefore remain the single largest party. But against the combined Opposition of the National Front, the radical Hindu BJP and the Marxists, it is unlikely to be in a position to form a government.

With the balance of power shifting in the party from the north (where Congress suffered its major reverses) to the south (where it gained more seats than expected), and with uncertainty now over Mr. Gandhi's future, the party is in for a traumatic period. But it is still in a more buoyant mood to resist splits that if had dropped to below 150 seats, as

some had expected.

The National Front, the coalition of Opposition parties led by Mr. V.P. Singh and now the second largest group in the Assembly, did less well than it had expected. Its major reverse was that its regional partners - the Telugu Desam in Andhra Pradesh and the DMK in Tamil Nadu - were humiliated by Congress. This robs the Front of much of its claim to be a national party with strong roots in the regions.

Instead, the Front, as it emerges in the Assembly, will largely be composed of the northern-based Janata Dal - mainly farmers' interests and former Congressmen. The one advantage of this narrower base for Mr. V.P. Singh will be that it should be more cohesive and easier to control.

But the other setback for the Front is that, while it has emerged weaker than expected, its two partners in the campaign to defeat Mr. Gandhi have both emerged stronger.

The militant Hindu BJP party, which has grown in strength on the back of Hindu revivalism, will increase its presence in the Parliament from two to around 60. At the same time, the Marxists could obtain over 50 seats with Mr. Jyoti Basu's CPM party in West Bengal exceeding most forecasts.

A National Front spokesman last night, putting the best face on the party's disappointment, called the result a "verdict for coalition government". Party

leaders will meet in the next few days to see how this can be achieved.

But to achieve a majority in the new Assembly, the National Front seems likely to need the support of both the BJP and the Marxists. Mr. L.K. Advani, the BJP leader, said last night that his party would not join a government which had Communists in it. The Marxists have taken the same view about the BJP which they regard as playing a major role in increasing Hindu-Muslim tensions in northern India.

The prospect is therefore that the National Front will have to form a minority administration, looking for outside support from the BJP to the right and the Marxists to the left. This has always been regarded as the worst recipe for stability.

It will none the less be a situation that will encourage the National Front to seek defections from Congress in an effort to build a stronger centrist administration. This is what Mr. Singh has had in mind when he has talked about a "re-alignment of Indian politics".

The prospects of a National Front government holding together for long in such circumstances are not good. A similar Janata coalition that came to power in 1977 held together for two years. The unhappy memory of that experience may be a factor for stability this time round.

## Popular crusader convinced of emerging the victor

David Housego reports on the rise to prominence of Opposition leader V.P. Singh

WHATEVER doubts others may have had about his leadership qualities, Mr. Vishwanath Pratap Singh, the Opposition leader, has long been convinced that he would emerge as Prime Minister.

Ten months ago, travelling to Delhi on the same plane as some Congress leaders who began to taunt him about the divisions within the Opposition, Mr. Singh suddenly proclaimed in a loud voice:

"You wait and see. I will be the next Prime Minister of India."

This election campaign has enhanced his claims to the job. Among the senior Opposition leaders, he is now the only one with credibility as a national leader. Almost everywhere he has travelled in the northern Hindi speaking belt, he has been acclaimed by large crowds - in sharp contrast to Prime Minister Rajiv Gandhi seemingly anxious through their acclaim to anoint him as

their leader.

Mr. Singh's conviction that he will become Prime Minister stems in part from the sense of certainty that goes with his crusading zeal. He sees his mission as restoring the dignity of India's democratic institutions, bringing back honesty and moral values into public life and, more recently, removing some of the bitterness that has increasingly marked Hindu-Muslim relations.

The simplicity of his own

life-style - travelling by train and car though the campaign, often on his own and carrying a small suitcase - has underlined his attacks on Mr. Gandhi's Government over corruption and the Bofors scandal. He has plunged into the crowds and seemed to make himself familiar with their problems, again in contrast to Mr. Gandhi who has had to work with the handicap of massive security protection.

As an Opposition leader, Mr.

Singh's weakness has been that he has let party quarrels get out of hand and at times seemed unable to exert his own authority. His strength has been to work out what emerged as a successful long term strategy and then to ensure that his partners stuck with it.

As Prime Minister, the risk is that he will continue to be irresolute and indecisive. He will suffer from the weakness that he will have few men that

he can call his own in the new Parliament. He believes strongly in advancing by consensus and is therefore likely to replace Mr. Gandhi's highly personal Government with a more cabinet system of decision making.

Mr. Singh would bring to the job considerable experience of government. He was Finance Minister under Mr. Gandhi where he was responsible for the initial measures of liberalisation and for much greater

transparency in preparing the Budget.

In terms of economic management, he seems likely to give priority to curbing budget and balance of payments deficits that he sees as the cause of inflation and India's worsening domestic and international debt. He will need to take hard decisions rapidly because India's diminishing foreign exchange reserves are increasingly forcing it to look to a further loan from the IMF.

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OVERSEAS NEWS

# Cheney set to brief Nato on proposed US defence cuts

By David White, Defence Correspondent

MR DICK CHENEY, the US Defence Secretary, is expected this week to give Nato allies further indications of the extent and nature of the cuts being contemplated in the Pentagon's next annual budget, and their implications for Nato operations in Europe.

Nato defence ministers will at the same time seek to prepare the ground for the latest task of allocating the arms reductions being negotiated at the Conventional Forces in Europe (CFE) talks in Vienna.

Ministers from European allied countries will also meet in Brussels today ahead of tomorrow's meeting of the alliance's Defence Planning Committee, including the US and Canada. The meeting has to undertake an annual force review, examining perfor-

mances over the last year and committing each country to set force levels for 1990.

The problem it now has to address is how to square this with the cuts in equipment and in US stationed manpower forecast in the CFE proposals.

British officials said they expected a CFE agreement to be signed next autumn. But there was still too much uncertainty on the size of alliance-wide cuts to be able to foresee the implications for individual members.

The officials made clear that the US would resist discussion of British force levels in West Germany, which are not affected by Nato's current CFE proposals.

At the same time, Mr Tom King, UK Defence Secretary, will urge European allies not

to anticipate arms control by cutting their commitments.

Britain believes the US can be seen as an exceptional case because of the extent to which it built up its military in the early 1980s.

The ministers will discuss a new Nato report on the need to reduce further the US current account deficit. It projects a decline in the deficit to \$109bn in 1990 from \$116bn in 1989 and \$126.6bn last year.

However, it said exclusive reliance on monetary policy could create stresses in the US financial system because of the presence of highly leveraged companies. It also expressed concern that high levels of corporate debt might deepen any slowdown in the economy resulting from tight monetary policy. In the medium term, the sole use of monetary policy to contain inflation could deter capital spending and impede exports, the OECD believes.

The OECD also fears that in the absence of fiscal action the US could remain over-dependent on foreign saving which could decline as the economy slowed in which case the tight

# OECD REVIEW CALLS FOR TAX OVERHAUL

# US urged to remove obstacles to savings

By Peter Norman, Economics Correspondent

THE Organisation for Economic Co-operation and Development has called on the US to carry out radical changes in its tax system to remove impediments to saving.

In its first review of the US economy since May 1988, the OECD said the US should mount a "two-pronged attack" in the fiscal policy area.

It said the US needed to cut its budget deficit by tightening expenditure control procedures. The US should also consider structural tax measures to improve the allocation of resources and raise private saving.

The Paris-based think tank, which is owned by the world's 24 leading industrial nations, said it foresaw growth in the US continuing at about 2.5 per cent in the second half of this year and in 1990, with inflation stabilising at around 6 per cent and only a small rise in unemployment from its current rate of around 5.3 per cent.

But it warned that there were risks "on both sides of such a prospect". The OECD said that investor confidence could decline as the economy slowed in which case the tight

monetary policy needed to combat inflation could induce a recession.

On the other hand, there could be a spontaneous recovery in consumer spending that would exacerbate inflationary pressures. The OECD said US monetary policy must remain tight to contain inflation and reduce further the US current account deficit. It projects a decline in the deficit to \$109bn in 1990 from \$116bn in 1989 and \$126.6bn last year.

However, it said exclusive reliance on monetary policy could create stresses in the US financial system because of the presence of highly leveraged companies. It also expressed concern that high levels of corporate debt might deepen any slowdown in the economy resulting from tight monetary policy. In the medium term, the sole use of monetary policy to contain inflation could deter capital spending and impede exports, the OECD believes.

The OECD also fears that in the absence of fiscal action the US could remain over-dependent on foreign saving which could decline as the economy slowed in which case the tight

	1988	1989	1990
GDP	4.4	3.0	2.5
Private consumption	3.4	2.4	2.0
Government consumption	0.4	2.6	1.3
Private fixed investment	5.8	3.6	5.1
residential	-0.3	-1.2	1.0
non residential	8.4	5.5	6.7
Exports: goods & services	17.8	11.4	8.0
Imports: goods & services	6.8	6.0	6.3
Current account (\$bn)	-126.6	-116.0	-109.0
Consumer prices	3.9	4.6	4.7
Industrial production	5.7	3.4	2.2
Unemployment rate	5.5	6.2	6.3

Source: US Department of Commerce, OECD Projections

resorting earlier this year to unilateral action against Japan, India and Brazil when it specified that they had acted as unfair traders under the "Super 301" provisions of the 1988 omnibus trade act. The report said the US should adhere to the dispute procedures of the General Agreement on Tariffs and Trade when it objected to the trade and industrial practices of foreign countries.

In a review of US industrial performance, the OECD said a number of structural impediments stood in the way of bet-

# Norway may lift oil output curb

By Karen Fosell in Oslo

THE Norwegian Government is coming under growing pressure to abandon its 7.5 per cent curb on crude oil production which was imposed in February 1987 in an effort to help the Organisation for Petroleum Exporting Countries stabilise world oil prices at \$28 a barrel.

Norway is Western Europe's second largest oil producer after Britain.

The 7.5 per cent production restraint removes about 120,000 barrels a day from world crude oil markets. Norway currently produces about 1.55m b/d. This could rise to 1.7m b/d next year if the curb were removed.

The former minority Labour Government, led by Mrs Gro Harlem Brundtland, implemented the oil production cut after a steep fall in world crude oil prices to below \$10 a barrel

in 1986. The production restraint policy is reviewed biannually and officials maintain that their policy on the issue is "flexible".

In 1986 the Government believed that by supporting the cartel oil prices would improve and help Norway's oil-dependent economy, which suffered heavily from the fall in price of crude oil.

Oil prices have recovered to above \$18 a barrel but Norway's economy is still struggling.

Unemployment is running at its highest level since the Second World War and state coffers could use the additional revenue arising from higher oil production.

In addition, Statoil, the Norwegian state oil company, has experienced financial difficul-

ties for the last three years. Now that oil prices have improved, it is planning to step up investment. Improvements in the oil price have also contributed to Statoil's earnings this year.

Analysts believe that the world crude oil market is strong enough to withstand continued production over Opec's self-imposed quotas. Prices have remained stable and above \$18 b/d for most of this year.

Norway is expected to decide its oil production restraint policy before Christmas and officials believe that the environment this year has changed significantly enough for new thinking about the cut to prevail.

# El Salvador suspends relations with Nicaragua

By Tim Coone in El Salvador

EL SALVADOR yesterday suspended diplomatic and commercial relations with Nicaragua following the discovery of an arms shipment of 24 surface-to-air missiles on a light aircraft which allegedly came from Nicaragua.

President Alfredo Cristiani, the Salvadorean president, said: "This is a dangerous escalation of the conflict," and he has called for the next meeting of the Central American presidents to be moved from Nicaragua.

"El Salvador will not go to the invitation of Nicaragua," he said.

El Salvador is also calling for emergency meetings of the UN General Assembly and the Organisation of American States.

The crash of the light aircraft has provided the first firm evidence that SAMs may now be in the hands of the guerrillas and according to a senior El Salvadorian army officer "this could change the

course of the war."

The missiles use infrared tracking devices to lock on to the exhaust emissions of aircraft of helicopters. The El Salvadorian air force is not thought to have effective counter-measures equipment fitted to its aircraft.

The first phase of a nationwide guerrilla offensive launched 15 days ago, was eventually beaten back with the extensive use by the armed forces of aircraft and helicopter

gunships. They are widely thought to be regrouping and preparing for another, possibly even heavier, offensive.

The arrival on the scene of SAM missiles for the first time in the 10-year-old civil war, would confirm the view that the guerrillas are aiming to seize and hold an important piece of territory in El Salvador.

The eastern part of the country, focusing on the city of San Miguel, is considered a highly

probable target.

The aircraft carrying the 24 missiles was a twin-engined Cessna with its registration painted out. Twenty three of the missiles were Soviet-made SAM-7s of which Nicaragua is thought to have several hundred, while the other was a US-made "Red-Eye." The US Government has supplied such missiles to the Nicaraguan Contras, a number of which have been captured by the Nicaraguan army.

# Opec ministers fail to reach production accord

By Steven Butler in Vienna

OIL MINISTERS from the Organisation of Petroleum Exporting Countries meeting in Vienna yesterday failed to make apparent progress toward reaching a production agreement for the coming year.

Delegates said there was resolve to reach a new agreement that would stop " rampant cheating" on quotas. But there had yet to emerge a basis for serious negotiations. Fears exist that oil prices could slump in the new year unless Opec output is reduced significantly from its present 23.5m barrels a day.

Foremost among obstacles to agreement was a demand by the United Arab Emirates to be

allocated a production quota of 1.9m b/d, against its current quota of just over 1m b/d. This was considered out of the question, given the expected size of the oil market in the new year and demands by other Opec members for increased quotas.

According to one proposal which appears to have broad backing from Gulf producers, the UAE and Kuwait would be given quotas of 1.5m each, and Opec's production ceiling would rise 2m b/d to 23.5m b/d. Some Opec members are having difficulty accepting Saudi Arabia's insistence that its 24.45 per cent share of Opec's production ceiling should not fall in any quota reallocation.

# Japan takes Hawaiian to its heart

By Ian Rodger in Tokyo

IN comparison with Mitsubishi Estate's purchase of New York's Rockefeller Center last month, the victory yesterday by an American in Japan's final sumo tournament of the year probably does not rank as a momentous event.

But for a time, American and Japanese seem to be able to find more reasons for distrusting and dishing each other, it provided an opportunity for both sides to show a little symbolic warmth for each other. And both rose to the occasion.

The victor, a 222kg (35 stone) Hawaiian by the name of Salevan Aitiano, burst into tears within seconds after he had thrust his final opponent out of the ring yesterday to become only the second foreigner in history, and the first in 17 years, to win a top sumo tournament.

Mr Aitiano, who is 25, tried desperately to conceal his emotions by wiping his face repeatedly with a cloth, but it took him several minutes to compose himself. "This has been my dream, I'm really stunned," he whispered later in fluent Japanese.

Japanese sumo fans, who in the past have not exactly welcomed foreign athletes into their national game, were touched. They were profuse in their applause when Mr Aitiano won, when he rose to collect the empress collection of cups, trophies and scrolls which goes to the winner and when he led the traditional tournament closing parade through Fukuoka.

The victory was especially sweet for Mr Aitiano, known as Kambishi in the ring. He arrived in Japan seven years ago and rose very quickly through the ranks of professional sumo to become the first foreigner to reach the second highest level, called ozeki, two years ago.

Then, he faltered - suffering a succession of injuries and ailments and performing listlessly in the ring. Critics wondered if, as on a couple of occasions in the past, the Japanese sumo establishment had found a way to prevent a foreigner from getting too far. Others said he had simply become bored.

If he had not won a majority of bouts in the current tournament he would have lost his ozeki status, but from the opening day two weeks ago it was clear that he had recovered his old form, often jumping up and down like a man with a third of his weight while going through the ritual preparations for his bouts.

Now he faces the prospect, if he wins another tournament, of being the first foreigner to become a yokozuna (grand champion).

How the Japanese would react to that remains to be seen. But the warm reception given Kambishi's victory yesterday is not the only sign that they are shedding their feelings about foreign athletes.



# Swiss vote to keep army

By William Dullforce in Geneva

SWITZERLAND decided yesterday to keep its army, even though more than 1m of its population voted for its abolition in a referendum that attracted an unusually high turnout of more than two-thirds of the electorate.

The score, 55.6 per cent in favour of dismantling the militia army, is a remarkable triumph for Young Socialists who raised the call for a referendum three years ago.

Their initiative was then dismissed as crazy in a country where armed neutrality has been the cornerstone of foreign policy for 170 years and where almost all adult males up to 55 keep a uniform and a weapon.

The proposal that the sentence "Switzerland has no

army" be written into the federal constitution was duly rejected by 64 per cent of those voting. But Mr Kaspar Villiger, the Defence Minister, had warned that a vote of one-third in favour of the proposal would weaken Switzerland's international standing.

Greatest support for the proposal appears to have come from young voters - a factor which indicates growing objections among those who have just started their military service. Some older Swiss voted against the proposal, not because they want to do away with the army but to protest against heavy spending on sophisticated new weapons.

# Japanese construction firms settle 'bid rigging' cases

By Ian Rodger in Tokyo

TWO highly publicised cases of unfair trading practices by Japanese companies, which have caused considerable embarrassment to the Japanese authorities, have been settled with unusual speed.

Last week, a group of Japanese construction companies agreed to pay the US Government \$4.7bn (\$4.1m) following accusations that the group had rigged bids for carrying out \$20bn worth of work on various projects at a US naval station south of Tokyo between 1983 and 1988.

In May, Japan's fair trade commission, following an investigation, imposed penalties on 70 companies for agreeing in advance on how to bid for the contracts. The US then claimed \$7bn from 140 companies allegedly involved in the bid rigging and threatened to take them to court.

Bid rigging in the Japanese construction industry is one of the main issues raised by the US in the Structural Impediments Initiative (SII) talks aimed at removing structural barriers to balanced trade in both the US and Japan.

Under a memorandum

signed by 89 Japanese construction firms and the US government, companies doing business or having assets in the US will pay the \$4.7bn by Dec 20. The remaining 41 firms did not join the agreement.

Meanwhile, the Fair Trade Commission has reprimanded Fujitsu and NEC, two leading computer manufacturers, for making abnormally low bids for computer system contracts. The reprimand follows the revelation last month that Fujitsu had won a tender for a computer system to control Hiroshima's municipal waterworks with a ¥1 bid.

Subsequent investigations revealed that NEC had won a contract in another public sector competition recently with a ¥1 bid, and five other similar cases in the past two years were discovered.

The cases had aroused international interest because they showed that huge Japanese electronic companies were prepared to suffer very large losses in the short term to build market share. The Commission said the practice was prejudicial to small competitors in the industry.

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EASTERN EUROPE

The party of the working class runs out of excuses

Czechoslovakia's Communist Party is falling apart fast as the world of pre-post-communism arrives, reports John Lloyd

THE television shows a man standing on a balcony above a factory yard in which a few hundred workers await his words. The camera is in close shooting his eyes flickering, his head nervously jerking to and fro.

was that the party of the working class no longer has an ally. For the past week, its leadership has grasped at the hope that the daily manifestations really were confined to the intelligentsia, young and old, and that the inverted torch which had settled on Czech society for the past two decades would reassert itself on the firm rock of proletarian indifference.

Already, the Communist Party has - ambiguously - talked of free elections, a new constitution and new laws on assembly and the press. Article 4 of the present constitution, which enshrines the party leadership role, is now "likely" to go.

The party has grabbed at the chance of round-table talks: Mr Urbánek has promised government posts for non-party and other-party people; and an investigation has been mounted into the beatings which the special internal ministry forces meted out to the demonstrators on November 19.

Only the gathering rebellion among over 1m members and the continuing occupation of the streets (at six degrees below) forces them to lurch from concession to re-arrangement. Last night, both the Slovak and the Federal Central Committees were again in session, cutting throats, and hoping that the bodies they will throw out to the public will get them indoors again.

For themselves," he cried yesterday. He has rejected all talk of future personal power. But even if he does not return to a writer's solitude, he will remain the moral centre of the drive to democracy.

What a coming of age! Prague has woken, after 21 years, to roaring festivals of improvisation, free speech and mass rejoicing. It is no cliché to say that the people are both engaged in the political events and polite, even affectionate toward each other.

More than 150,000 people carrying portraits of Pope John Paul marched through the west Ukrainian city of Lvov yesterday demanding the legalisation of the Ukrainian Catholic Church. Reuter reports from Moscow.

SOVIET REACTION

Papers give subdued reports of events

THE speed of events in Eastern Europe, above all in the conservative Communist states of Czechoslovakia and East Germany, has for once left Soviet commentators almost speechless.

The resignation of Milos Jakes, the Czechoslovak Communist Party leader, was disposed of in just one paragraph with the attention focused on the new party leadership.

MR LADISLAV ADAMEC, the Prime Minister of Czechoslovakia who refused to join the new pollitburo on Friday night, saying that he could not support such a team, has been practically disowned by the party leadership. But he is now slowly finding a new home among the Civic Forum.

party ranks. He seems to have kept his head fairly low during the Prague Spring movement, for which he was rewarded in 1970 by being appointed deputy prime minister of the Czech Lands region, a post he held for 13 years. In 1977, he was elected prime minister of the region and the following year he was made prime minister of Czechoslovakia.

Yet Mr Gorbachev still refused to commit himself to any rigid prescription of the future face of socialism. He denounced "populist demagoguery" and "nationalist or chauvinist trends", saying: "At the present complex stage, the interests of the consolidation of society, and the concentration of all its sound forces on the accomplishment of the difficult tasks of perestroika, prompt the advisability of keeping the one-party system."

He can play a role in the transition." His supporters say that he tried to resign as early as June, an offer which was repeatedly turned down.

They include France's Credit Lyonnais, which is also head of a French consortium set up in July, of which ESD is a member, to encourage joint ventures in the Soviet Union. While the Soviet partners were keen at the time to set up a joint venture in simple wholesale banking, observers said they were also eager to acquire Western banking technology.

Leipzig steam plant order. East German companies at the weekend a DM252m (£78m) order for two West German companies to build a steam generation plant for modernising the Buna chemical works near Leipzig. David Marab reports from Bonn.

REUNIFICATION

Weizsäcker proposed to lead unified Germany

THE CHAIRMAN of one of East Germany's new opposition parties has suggested making Mr Richard von Weizsäcker, the West German president, head of state of a united Germany.

unity is not on the agenda at the moment, as it would damage stability in Europe. However, Mr Egon Krenz, the East German leader, told the Financial Times on Friday that a confederation would be an eventual possibility as part of a future "Common European Home".

THE East German Socialist Unity (Communist) Party has suffered a stunning setback in an official poll showing that only 19 per cent of adults would vote for the party if elections were held now.

with the opening of the borders to the West. East Germany introduced strict customs measures last Friday to curb the smuggling of subsidised consumer goods to the West and to Poland.

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Czech Premier Ladislav Adamec at a meeting of opponents of the government in Prague yesterday

CZECHOSLOVAKIA'S PRIME MINISTER

Adamec finds a cautious home among reformers

By Judy Dempsey and John Lloyd in Prague

SOVIET SOCIALISM

Gorbachev backs continuing monopoly for party

By Quentin Peel in Moscow

PRESIDENT Mikhail Gorbachev yesterday issued a resounding call for the Communist Party to maintain its monopoly role in a pluralistic Soviet society, as part of an attempt to present a new vision of a future democratic socialism.

MAZOWIECKI IN SOVIET UNION

Polish Premier's visit recalls Katyn massacre

By Christopher Bobinski in Katyn

MR Tadeusz Mazowiecki, Poland's premier, yesterday attended a church service at Katyn, the site of a wartime massacre of more than 4,000 Polish officers interned in 1938, as part of his four-day visit to the Soviet Union.

EAST GERMAN PARTY

Poll of no confidence in Krenz

By Leslie Collitt in Berlin

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BULGARIAN SECRET

Police unit to go

Bulgaria's new Communist leadership, anxious to show they are reformers, say they will disband a feared secret police unit used to spy on dissidents.

SOVIET UNION

Optimism on co-operation

Mr Helmut Haussmann, the West German Economics Minister, said yesterday that the chances for economic co-operation between the two Germanies were much better than generally assumed, even without big changes in the East German political and economic system.

SOVIET UNION

Polish Premier's visit recalls Katyn massacre

By Christopher Bobinski in Katyn

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BULGARIAN SECRET

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UK NEWS

Pound faces further pressure on foreign exchanges

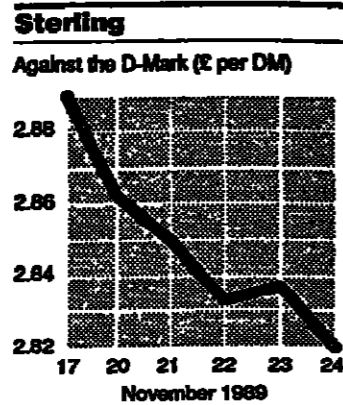
Major firm on use of interest rates

By Patrick Harverson, Economics Staff

THE POUND is likely to come under further pressure on the foreign exchanges this week in spite of yesterday's assurance by Mr John Major, the Chancellor of the Exchequer, that he was ready to raise bank base rates further in the fight against inflation.

Mr Major, speaking yesterday on the Channel 4 programme *Answering Back*, said: "If it is necessary in the wider judgment to use interest rates by raising them again to bear down on inflation, then of course I will do that. Inflation is the first priority and we must seek to bring that down."

It has been the markets' lack of confidence in the Government's apparent willingness to take the politically unpopular course of increasing rates again, allied to pessimism about the economic outlook, that has undermined the pound. Last week sterling fell 7 pence against a strong D-Mark, to DM2.32, its lowest level for more than 24 years.



John Major

Aware of widespread concern that the economy is being wounded by high interest rates, the Chancellor sought yesterday to allay the fears of the business community and the City of London that the economy is being pushed into recession.

He said that the forecast of 1 1/2 per cent economic growth next year, carried in the recent statement on Government expenditure plans, was not a prediction of recession. He said: "What will happen over the next year or so is that growth will continue, but at a modest rate."

Speaking on the subject of fiscal policy during the Channel 4 programme, Mr Major confirmed that there was little chance of fresh income tax cuts next year.

He said: "I don't know whether we'll be able to proceed with reducing taxes in the next Budget, or the Budget thereafter. We will have to see what progress we make with inflation."

The City had been alerted last week to the likelihood that there would be no reduction in the tax burden in the Budget next March when the traditional reference to the expectation of income tax cuts was omitted from the Queen's Speech.

CBI details: Page 10

interest rates used by Mr Nigel Lawson, Mr Major's predecessor as Chancellor, has been quietly shelved. Some City of London analysts are convinced that Mr Major is prepared to let the markets decide the fate of the pound. The alternative would be a rise in interest rates to support sterling.

Analysts regard such a move unlikely because it would inflict further political damage on the Government at a time when the Prime Minister was facing a challenge to her leadership, and the Conservatives were falling further behind Labour in the opinion polls.

Sterling's decline in recent weeks has been exacerbated by the gloomy outlook for the

economy. The Confederation of British Industry, the employers' organisation, says in its monthly trends survey for November, published today, that British business is increasingly pessimistic about the future.

Companies are reporting the worst outlook for orders for over two years, reduced demand for exports, and a growing accumulation of stocks, according to the survey. In its latest forecast for the economy, also published today, the CBI predicts that the next two years in Britain will see slow overall economic growth, an end to the investment boom in manufacturing industry, and flat company profits.

Deutsche Bank deal expected

By David Barchard

MORGAN GRENFELL, the London merchant banking group, is expected to announce today that it has struck a deal with Deutsche Bank, after a weekend of last-minute negotiations to fend off a likely takeover bid from Banque Indosuez of the French bank.

Mr John Craven, Morgan Grenfell's chairman, has to announce a deal by Wednesday, when shareholders at Willis Faber, the insurance broker, vote on whether to sell a further 10 per cent of Morgan Grenfell to Banque Indosuez at 482p a share.

Mr Craven is thought to have spent the weekend trying to persuade Deutsche Bank to make a bid at 55 a share, valuing the group at just under 2800m (\$1.26bn). The deal would involve at least one other institution.

Indosuez, which wants to form a pan-European banking group, became the largest single shareholder in Morgan Grenfell on October 26. However, the price Indosuez is offering Willis Faber shareholders is 14p under last Friday's closing price of 476p.

Morgan Grenfell's management has been determined to prevent the French bank becoming dominant among its shareholders.

Polls put Labour further ahead as Thatcher faces challenge

By Michael Cassell, Political Correspondent

PRESSURE aimed at averting a damaging challenge to Mrs Margaret Thatcher's leadership will intensify at Westminster this week in the run-up to the Thursday deadline for nominations from any challengers.

At the start of what inevitably will be a tense and anxious week for the government, there was further bad news in the shape of new opinion polls putting the Labour opposition party still further ahead and confirming recent indications that Mrs Thatcher herself is increasingly regarded as an electoral liability.

No challengers to the Prime Minister have yet formally announced their intention to stand, although Sir Anthony Meyer, the MP for Clwyd North-West, yesterday repeated his readiness to challenge the Mrs Thatcher if no one else came forward.

Mr Christopher Patten, the Environment Secretary, said that Sir Anthony's challenge was "bad for the country and certainly bad for the Conservative party".

He said it would be "profoundly dishonourable" for a former minister in Mrs Thatcher's administration to do other than argue and fight vigorously for her to continue.

Some MPs last night suggested that Sir Anthony



The Prime Minister

on BBC television tonight. Though government whips accept they can bring little direct pressure on Sir Anthony to withdraw, they will be stepping up last-minute efforts to drive home the message to all MPs - either potential candidates or their supporters - that there should be no contest.

The main interest among Tory MPs this week will be to see whether any more substantial contestant decides to step forward before Thursday and then persuade a sufficient number of colleagues to register a strong enough protest on the following Thursday to undermine Mrs Thatcher's position.

According to a Mori poll in yesterday's Sunday Times newspaper, the Labour opposition lead the Tories by 14 percentage points, with 51 per cent support against 37 per cent for the government.

Labour's rating is the highest since Mrs Thatcher became prime minister and its biggest lead since November 1980.

The same poll shows that one in four Conservative supporters believe Mrs Thatcher should stand down before the next election.

Mr Michael Heseltine, the former Defence Secretary, emerges as the most popular alternative.

Sex equality report urges pay reforms

By Lisa Wood, Labour Staff

UNIONS and employers have not yet sufficiently widened the agenda of collective bargaining in order to tackle sexual discrimination at work, according to a report published today by the Equal Opportunities Commission.

The report comes at a time when many unions say they are putting more effort into changing bargaining to include women's issues. But the report, which examines the engineering, food and knitwear industries, indicates that the status quo still largely prevails in these industries.

The report, which follows an earlier study which pointed to the need for improved statutory provisions, argues that both employers and trade

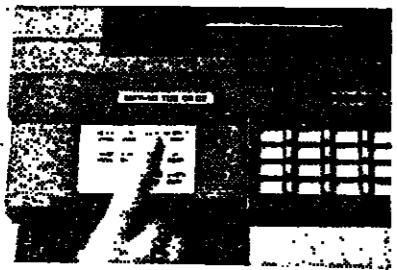
unions should "see the sense, as well as the justice" of tackling sexual discrimination. This would mean, in many organisations, integrating equal opportunity policies with the collective bargaining.

"The case studies reveal that the bargaining agenda are invariably narrow with pay as the most important and often the only item. Negotiators focus on increases in basic pay without questioning whether the existing pay or grading structures are fair to both sexes," the report says.

Negotiations were handled by men, and issues of particular importance to women were often perceived by their unions as minority rather than members' interests.

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UK NEWS

Oftel faces legal challenge from games company

By Hugo Dixon

SIR Bryan Carsberg, the director general of the Office of Telecommunications, is facing a court challenge, indicating that he overstepped his authority in passing stiff regulations to control interactive telephone services.

which are used for various types of promotions. Computertel, a privately owned company with turnover of £2.5m last year, said its business was threatened by Sir Bryan's decision in July that interactive services lasting more than five minutes could be offered only if they conformed to a strict code of practice.

'Green' tax planned to meet cost of pollution

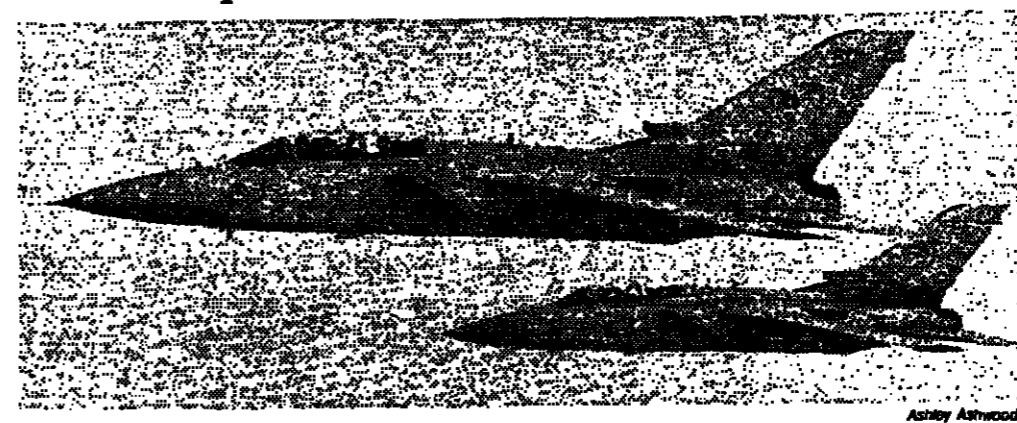
By John Hunt, Environment Correspondent

A "GREEN tax" may be imposed on fossil fuels such as coal and oil in order to pay for the costs of the atmospheric pollution they cause, Mr Chris Patten, the Environment Secretary, said yesterday.

Cash flow trouble in 'arms sale of century'

Andrew Gowers finds the euphoria of a £15bn deal with Saudi Arabia is diminished

WHEN a significant expansion of Britain's Al-Yamamah defence contract with Saudi Arabia was announced in July last year, many observers were quick to hail it as "the arms sale of the century."



Tornadoes for crude: but since the deal was struck oil has become "devalued currency"

which Saudi Arabia is largely paying for equipment. Under a barter arrangement in force since the contract began, Royal Dutch/Shell and British Petroleum have been lifting 400,000 barrels a day (b/d) of Saudi crude and paying the proceeds into a Ministry of Defence account, from which relevant payments are passed on to the contractors.

ment supplied and the flow of money from Saudi crude. Concern about the risks involved in the barter deal even prompted the National Audit Office, Parliament's financial watchdog, to launch its own discreet inquiry last spring.

the contract, is supposed to deliver more than 100 Tornado fighters - including interdictor-strike (IDS) aircraft and the so-called air defence variant (ADV) as well as P400 trainers and Hawk 300 trainers. About 30 of the Tornados and many of the training aircraft have been delivered so far.

whether the Saudi Government will want to proceed with these parts of the contract. The current difficulty poses awkward dilemmas for Saudi Arabia, which has placed heavy emphasis on defence spending in spite of the recent years of recession and a chronic budget deficit.

Mercury must share BT's subsidy costs

By Hugo Dixon

MERCURY Communications, British Telecom's smaller rival, will soon have to pay its share of the bill for subsidising loss-making rural phone services, according to the Office of Telecommunications, the industry's regulatory body.

Bryan said he had always made clear that he would give Mercury a share of the social obligations when its business had progressed beyond the start-up phase, and that time was now rapidly approaching.

Multi-track EC plans for 1992

By Robert Mautner, Diplomatic Correspondent

A MULTI-TRACK European Community, with curbs on the powers of the European Commission and different groups of countries coming together on different priorities, is proposed in a report published today by the Institute of Economic Affairs.

Fraud cases on the increase, report finds

By Alan Cane

FRAUD against large UK companies, especially those in the financial sector, is both substantial and on the increase, a report claims.

DISHONEST employees and managers are costing the retail industry more than £20m a year, a Manchester conference was told last week, writes Martin Regan.

between 1.5 per cent and 5 per cent of annual turnover reported through theft by customers' staff.

dealing, which in turn was seen as substantially worse than the dishonest making of multiple share applications.

Unionists in election challenge

NORTHERN IRELAND'S two main unionist parties are to challenge each other in future general elections for seats which nationalists are deemed to have no chance of winning.

BA executive stays

MR Michael Batt, head of central marketing at British Airways, has changed his mind about leaving the company to take a position at Virgin Atlantic.

Talks consider London road jams

By Kevin Brown, Transport Correspondent

LONDON'S rival Conservative and Labour local authority associations will join academics and businessmen today at a convention - highlighting cross-party concern over the capital's transport difficulties.

fall from 11mph to 9-10mph over the next decade unless the Government accepts the need for radical improvements in public transport and controls on private car use.

have been put off, including a proposed east-west Crossrail scheme for a link with British Rail freight tunnels from Paddington to Liverpool Street.

Government fears setback in Docklands

By Hazel Duffy

THE GOVERNMENT has expressed fears that the revival of London's Docklands, the centrepiece of its plans to revive the inner cities, may founder because of a downturn in the economy.

Students lobby banks over college loans

By David Thomas, Education Correspondent

THE NATIONAL Union of Students will begin a series of protest actions this week designed to persuade the banks to drop their participation in the Government's proposed student loans scheme.

for a Student Loans Company, which will administer the loan scheme due to be introduced next September.

this week to the offices of some 800 student unions asking them to launch a series of actions that will include:

Boeings 'safe'

A WRITING FAULT discovered in British Airways' five Rolls-Royce-powered Boeing 747-400 aircraft is not a threat to safe operation, the airline stated yesterday.

Welsh investment

TWO Japanese companies, Dynic Corporation and C.Roh, are to join forces in a venture to produce printer ribbons in Cardiff.

Conference City advertisement for Birmingham. Features a large graphic of a heart shape and text: 'From 15 to 15,000. Birmingham is Conference City. The Big Heart of England. Right at the hub of the national road and rail networks. And less than two hours by air from most European capitals. It has a choice of over 170 specialist locations for meetings from 15 to 15,000. Including the £150 million International Convention Centre, Europe's most modern purpose built conference centre.'

Foreign tourists likely to reach record numbers

By David Churchill, Leisure Industries Correspondent

BRITAIN is on course to receive a record number of overseas visitors this year, according to figures to be published this week by the Government.

• A cut in the operations of charter airlines, including the disposal of surplus aircraft and the leasing of others to airlines outside the UK.

Advertisement for Les Freres Tilouche restaurant. Text: 'Les Freres Tilouche announce the opening of Le Qual Restaurant at 1 Broken Wharf St Paul's Vista London EC4V 3QQ. Open: Breakfast, lunch, dinner & private functions. Tel: 01-588 7559.'



16/11/89

UK NEWS

# Midlands will go green with project for megaforest

Richard Tomkins looks at plans for Britain's first large-scale broadleaf planting since the New Forest

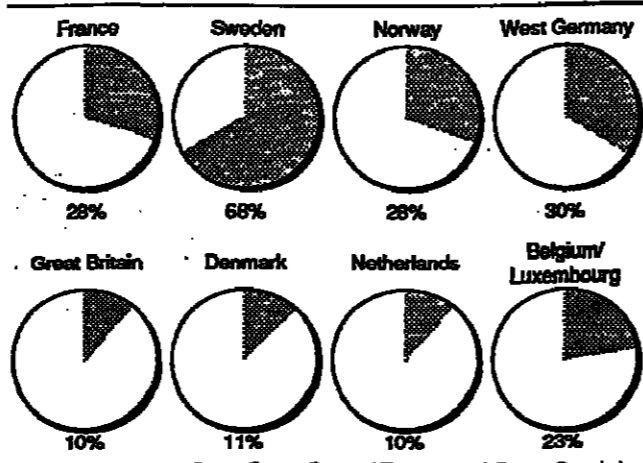
THE creation of hardwood forests is a rare event in Britain. The last time it was done on any large scale was in 1097 when William the Conqueror delineated the New Forest in Hampshire as a hunting ground. History, therefore, will be in the making today when the Countryside Commission announces its proposals for establishing another new forest. Like William the Conqueror's, this one will cover an area of about 150 square miles, but this time it will be somewhere in the Midlands.

There are sound commercial reasons for creating what has already been dubbed the megaforest. Britain, once a densely wooded island, has lost its trees to agriculture and industry over the centuries to the point where it has become the least forested country in Europe.

With an annual timber consumption of 60m tonnes, or 100m trees, Britain is able to meet domestically only 10 per cent of its needs. The result is an annual timber import bill of nearly £7bn to make up the difference - the country's fourth-biggest import bill after food, fuel and motor vehicles.

Commercial objectives, however, are not the main ones underlying the Countryside Commission's scheme. On the contrary, the commission

## Forestry as % of total land area



purpose lowland forests that would provide public amenities as well as commercial profit.

One practical proposal that came out of the review was for a series of 12 "community forests" of 40 to 65 sq miles each to be created on the outskirts of Britain's larger cities.

Plans for the first two, in south Staffordshire and south Tynes and Wear, were announced in July.

The second prong of the strategy was the megaforest itself. It is intended to combine all the most desirable aspects of a multi-purpose forest by

providing a recreational and tourism resource, enhancing the environment, providing opportunities for linked commercial developments, and contributing to the national timber supply.

The idea is to create not just a dense mass of woodland, but a blend of wooded areas, open country, villages, lakes and farmland. Leisure opportunities could include camping, cycling, water sports, adventure play areas, and nature trails.

The forest will not involve massive land seizures, but will

# Members of Fimbra launch revolt over running costs

By David Barchard

MEMBERS OF the Financial Intermediaries, Managers and Brokers Regulatory Association believe they are close to victory in the first serious revolt by members of a self-regulatory organisation since the Financial Services Act came into force in April last year.

Although the Fimbra council's proposals for a now abandoned compulsory professional indemnity insurance scheme lies at the heart of the storm, the rebels make clear that their basic objection is to the way Fimbra has been run under Lord Eiton.

Fimbra's annual meeting on December 13 will have four different resolutions on its agenda, each of which would make the position of Lord Eiton, Fimbra's chairman, and 15 members of the 21-member board untenable.

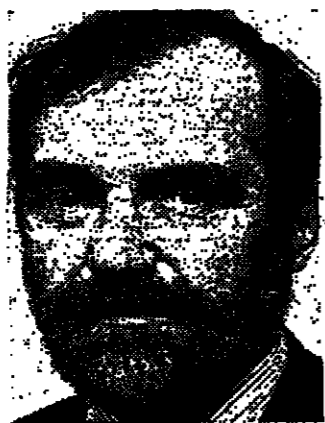
The most strongly worded of the resolutions directly calls on Lord Eiton and the 15 to go. More than 1,750 of Fimbra's 8,000 members have signed the resolutions, and more than 2,500 members have delivered proxy votes, supporting a resolution calling on Lord Eiton to resign.

Mr Andrew Paddick of the Institute of Insurance Brokers,

## APPOINTMENTS

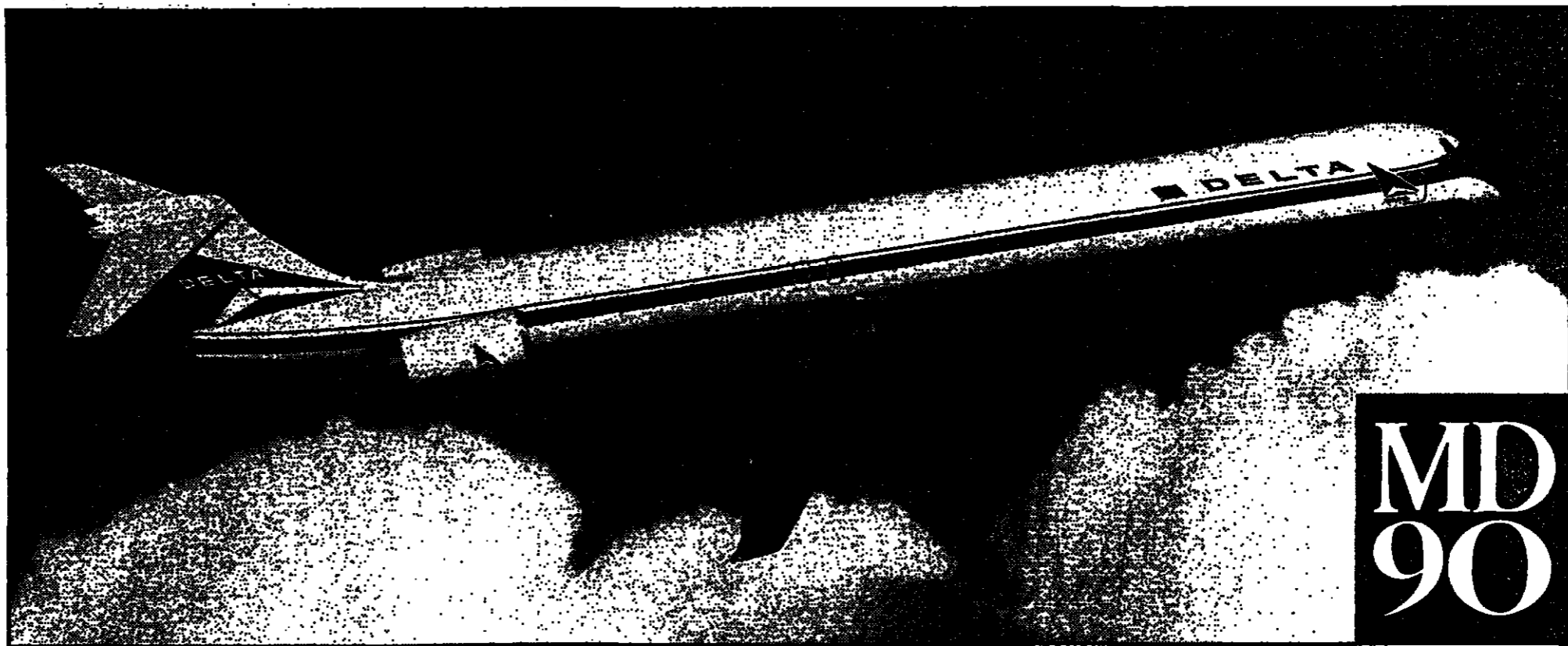
### Vickers managing director

- Mr Roger Foulkes has been appointed sales and marketing director of MONCASTLE WIRE PRODUCTS, part of Ash & Lacy. He was group marketing director, J. & T. Group.
- Mr Michael Collins has been appointed a director of ROYAL TRUST BANK.
- Mr G. Fransom has been appointed chief engineer of the ASSOCIATED OFFICES TECHNICAL COMMITTEE.
- NATIONAL & PROVINCIAL BUILDING SOCIETY has appointed Mr Andrew Newell as risk manager. He was bond market manager.
- Mr Colin Chandler has been appointed a director of VICKERS, and will succeed Mr R.D. Taylor as managing director on January 1. Mr Taylor remains on the board until he retires after the annual meeting in April.
- Mr Bob Munton has been appointed to the board of SPEARHEAD EXHIBITIONS. He joined the group in 1981.
- Mr Philip P.C. Gregory has been appointed group finance director and a managing trustee of MUTUAL MUTUAL INSURANCE. He was group finance director of Sema Group.
- Mr Rowland Leigh, SAVOY HOTEL group company secretary, has additionally been appointed finance director.
- MANUFACTURERS HANOVER CORPORATION has promoted the following from vice president to senior vice president at the London office: Mr Clifford J.M. Fairley, offices and services group; Mr Malcolm Frost, personnel; Mr Philip L. McRae, UK representative office; and Mr George V. Talav, eastern Europe group.



Mr Les Baker (above), technical director of Rechem International, has been elected chairman of the NATIONAL ASSOCIATION OF WASTE DISPOSAL CONTRACTORS.

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**FINANCIAL TIMES CONFERENCES**

The following conferences are among those to be arranged by the Financial Times:

**THE FOOD AND DRINK INDUSTRY IN EUROPE**  
28 & 29 November 1989 - London

**WORLD BANKING: EUROPE AFTER THE DELORS REPORT**  
30 November & 1 December 1989 - London

**WORLD TELECOMMUNICATIONS**  
4 & 5 December 1989 - London

**FINANCIAL TIMES/PRICE WATERHOUSE CAPITAL MARKETS WORKSHOPS**  
4 - 6 December 1989; 21 - 23 March 1990;  
16 - 18 May 1990;  
4 - 6 July 1990 - London

**WORLD PULP & PAPER**  
12 & 13 December 1989 - London

**CREATING A EURO-WORKFORCE IN THE 90s**  
22 & 23 January 1990 - London

**COMMERCIAL AVIATION IN THE ASIA-PACIFIC REGION TO THE END OF THE CENTURY AND BEYOND**  
12 & 13 February 1990 - Singapore

**CABLE TELEVISION & SATELLITE BROADCASTING**  
28 February & 1 March 1990 - London

**THE LONDON MOTOR CONFERENCE**  
5 March 1990 - London

**COMPETITION, MERGERS, ACQUISITIONS AND ALLIANCES IN EUROPE**  
13 & 14 March 1990 - London

**THE EUROPEAN WATER INDUSTRY**  
26 & 27 March 1990 - London

**WORLD PHARMACEUTICALS CONFERENCE**  
26 & 27 March 1990 - London

**VENTURE FORUM EUROPE '90**  
4 - 6 April 1990 - Paris

All enquiries should be addressed to:  
**Financial Times Conference Organisation**  
126 Jermyn Street, London SW1Y 4UJ  
Tel: 01-925 2323 (24-hour answering service)  
Telex: 27347 FT CONF G Fax: 01-925 2125

**CBI sees low manufacturing output in 1990**

By Peter Norman, Economics Correspondent

MANUFACTURING industry is suffering a slowdown in demand for its products and can look forward to only low output growth between now and the end of 1991, according to the Confederation of British Industry.

The confederation's industrial trends survey for November has found that more companies are reporting that their order books are below normal than at any time since October 1986.

The organisation's latest two-year forecast, also published today, points to two years of slow overall economic growth, an end to the manufacturing industry's investment boom and flat company profits as the Government's counter-inflationary policy depresses domestic demand.

The CBI monthly industrial trends inquiry - which polled 1,250 companies between October 24 and November 15 - found that export demand had weakened, with a marked increase in the proportion reporting that export order books were below normal.

Commenting on the findings, Mr David Woollam, chairman of the CBI's economic situation committee, said: "Any

further erosion in business confidence or a deterioration in export markets could bring us perilously close to recession."

More companies are reporting greater stock levels than at any time so far this year, pointing to an accumulation of unsold goods.

The survey also suggests that manufacturers will not be increasing their output over the next four months. On balance, only 1 per cent of companies expect to increase output between now and next March compared with 25 per cent a year ago.

The survey shows that 34 per cent of manufacturers now think their total order books are below normal, while only 17 per cent consider them above normal.

The employers' organisation said intermediate and consumer goods industries had reported order books "significantly below normal", with demand weakest for textiles.

The capital goods industry, in contrast, says that its overall orders are only slightly below normal.

However, capital goods manufacturers have experienced weak demand in foreign markets with large companies,

**EXTRACTS FROM THE CBI FORECAST**

	% change on previous year		
	1989	1990	1991
GDP (output)	2.2	1.4	1.8
of which manufacturing	4.8	1.3	2.3
Fixed investment	6.3	0.0	0.5
of which manufacturing	9.0	-0.1	0.2
Inflation (annual average RPI)	7.8	6.3	4.7
Exports: goods, services	5.2	5.6	3.3
Imports: goods, services	8.3	1.1	1.9
Current account (£bn)	-19.8	-18.8	-13.3
Stockbuilding (£bn)	4.4	-1.1	0.0

employing more than 5,000 people, reporting significant declines in export demand.

About the only bright spot in the survey is itself a reflection of the slowdown in demand: fewer companies expect to raise factory gate prices in the next four months than was the case a year ago.

Meanwhile, in its latest quarterly economic forecast, the CBI gives a warning that fixed investment in Britain will stagnate next year while company profits will show no real growth in either 1990 or 1991.

The CBI has revised its expectations of economic growth for next year down to 1.4 per cent from the 2.3 per cent rate envisaged in its previ-

ous forecast in August and has said it expects growth of only 1.5 per cent in 1991.

The CBI's 1.4 per cent growth forecast for next year broadly matches the 1.25 per cent growth rate forecast in the Government's recent Autumn Statement.

However, the CBI is somewhat more optimistic than the Government in projecting a decline in the annual rate of retail price inflation to 5.3 per cent by the fourth quarter of next year from 7.5 per cent in the current quarter. The CBI has forecast that retail price inflation will average just 4.7 per cent in 1991.

Analysts have interpreted the Autumn Statement as

implying that bank base rates will stay around their current 15 per cent level for most or all of next year. However, the CBI expects them to fall from 15 per cent to 12 per cent between the end of March and the end of 1990. It also assumes a further easing of base rates in 1991 to an average 11 per cent.

The CBI expects, too, that the Government will cut the standard rate of income tax to 24 per cent from 25 per cent in the 1991 Budget. It also expects a strong 5.8 per cent growth in the export of goods and services next year followed by 3.3 per cent growth in 1991.

Imports are forecast to grow by only 1.1 per cent in 1990 and 1.9 per cent the following year.

The balance-of-payments deficit on current account is expected to fall to £13.8bn next year from a forecast £19.8bn this year. However, the CBI has projected a high current-account deficit of £13.8bn for 1991, reflecting expected slackening of world trade growth and increased consumer demand in Britain after the income tax cut it expects in 1991.

The CBI expects hardly any growth in business investment in the next two years.

**Lloyds Bank forecasts cuts in tax**

By Peter Norman, Economics Correspondent

THE 1991 Budget is likely to see the British Government resuming its policy of tax reductions because it will be the last opportunity to influence the economy significantly before the next election, according to Lloyds Bank.

In the bank's latest UK Economic Outlook, Mr John Young, Lloyds' UK economic adviser, said the economy would hover on the brink of recession next year with growth decelerating to 1.5 per cent.

However, the outlook for inflation will remain poor, Mr Young added, with 5 per cent inflation becoming increasingly regarded as the norm for the UK economy in the early 1990s.

The bank said the Autumn Statement forecasts of a decline in the current-account balance-of-payments deficit to £15bn next year from £20bn in 1989 were realistic. It said a further slow improvement to a deficit of £12bn in 1991 was possible although the deficit was likely to rise again afterwards as domestic demand recovered.

**Fuel and energy companies fail to settle deal**

By Charles Leadbeater

BRITISH COAL and the electricity generating companies have yet to agree on a three-year coal supply contract, according to senior executives at the corporation.

The already tense relations between British Coal and National Power and PowerGen, the two generating companies to be created by the privatisation of the electricity supply industry, have been further strained by comments last week by Mr John Baker, National Power's chief executive-designate, that a three-year deal had been drawn up that would freeze domestic electricity prices over the next year.

A senior executive at British Coal said Mr Baker's comments were premature, within the outline structure of the deal, many details, including prices, remained to be settled.

**British Coal will develop land left by pit closures**

By Charles Leadbeater, Industrial Editor

BRITISH Coal is planning to move into property development to exploit the large vacant sites left by the pit closure programme it has conducted since the end of the 1984-85 miners strike.

The corporation's diversification into property development confirms a growing trend among large companies in industrial sectors that have contracted and restructured in the 1980s.

British Rail is involved in big developments at several central London stations. Associated British Ports, the country's largest port operator, earns about half its profits from property, while Sea Containers, the second-largest operator, last week announced a £200m development at Harwich docks and a £100m development at Felixstowe.

British Coal has long benefited from property disposals.

**Power sell-off seen as pushing price up 50%**

By Maurice Samuelson

THE LONG-TERM effect of privatising the electricity industry will be to push prices about 50 per cent higher than if privatisation were not to take place, two London Business School economists predict today.

That is because of the higher rates of return on capital that will have to be earned by the privatised successors of the CEGB.

Their conclusion contrasts with assurances by Mr Cecil Parkinson, as Secretary for Energy, that competition in power generation would reduce prices in the long term.

Under Mr Parkinson's plans, the corporation would provide the land as its contribution to joint ventures with agents or developers, who would provide the finance for the development. The corporation would eventually benefit from rental income.

**Advisers raise doubt over privatisation timetable**

By Maurice Samuelson

THE GOVERNMENT is being urged to revise its timetable for selling the various parts of the electricity industry to ensure that its privatisation is completed before the next General Election.

Under the present timetable, the two Scottish boards are due to be sold next August, the 12 distribution companies of England and Wales two months later, and the two big generating companies, National Power and PowerGen, in the spring of 1991.

The Department of Energy yesterday said there was "no question" of abandoning that timetable. However, Kleinwort Benson, the Government's chief advisers, are said to be examining a number of different options over timing.

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The Department of Energy yesterday said there was "no question" of abandoning that timetable. However, Kleinwort Benson, the Government's chief advisers, are said to be examining a number of different options over timing. The generating companies, while insisting that they will comply with the official timetable, are understood to favour being sold simultaneously with the rest of the industry. National Power said: "Providing the conditions are right, we would be enthusiastic to be privatised as soon as possible. But it is for the Government to decide."

**If you are a professional, you may well be interested in some of these events.**

Month	Period	CONGRESSES AND EVENTS IN 1st HALF OF 1990	Estimated Attendance	City
January	13 to 17	V International Congress of Physical Education		
	14 to 19	XII International Congress of Electromyography and Clinical Neurophysiology		
	30 to 8 February	VIII General Assembly World Lutheran Federation		
February	17 to 21	X International Symposium on Facial Surgery		
	18 to 22	FAABS - VI Congress Pan-American Association of Biochemical Societies		
March	6 to 8	I International Congress on Pediatric Nutrition		
April	18 to 21	II Latin American Symposium on Neurological Surgery on the ear and skull base		
	21 to 4 May	International Congress on Irrigation and Drainage		
	25 to 28	IV International Cataract and Intraocular Lens Symposium		
	29 to 4 May	International Conference on Transport Properties of Superconductors		
May	6 to 10	II Congress of the Latin American Association of Immunology		
	14 to 17	XXII World Congress of International Road Union - IRU		
	14 to 18	II Triomus - Triennial Museum Meeting of Rio de Janeiro		
June	16 to 21	L.E.S. International Conference - Licensing Executives Society		

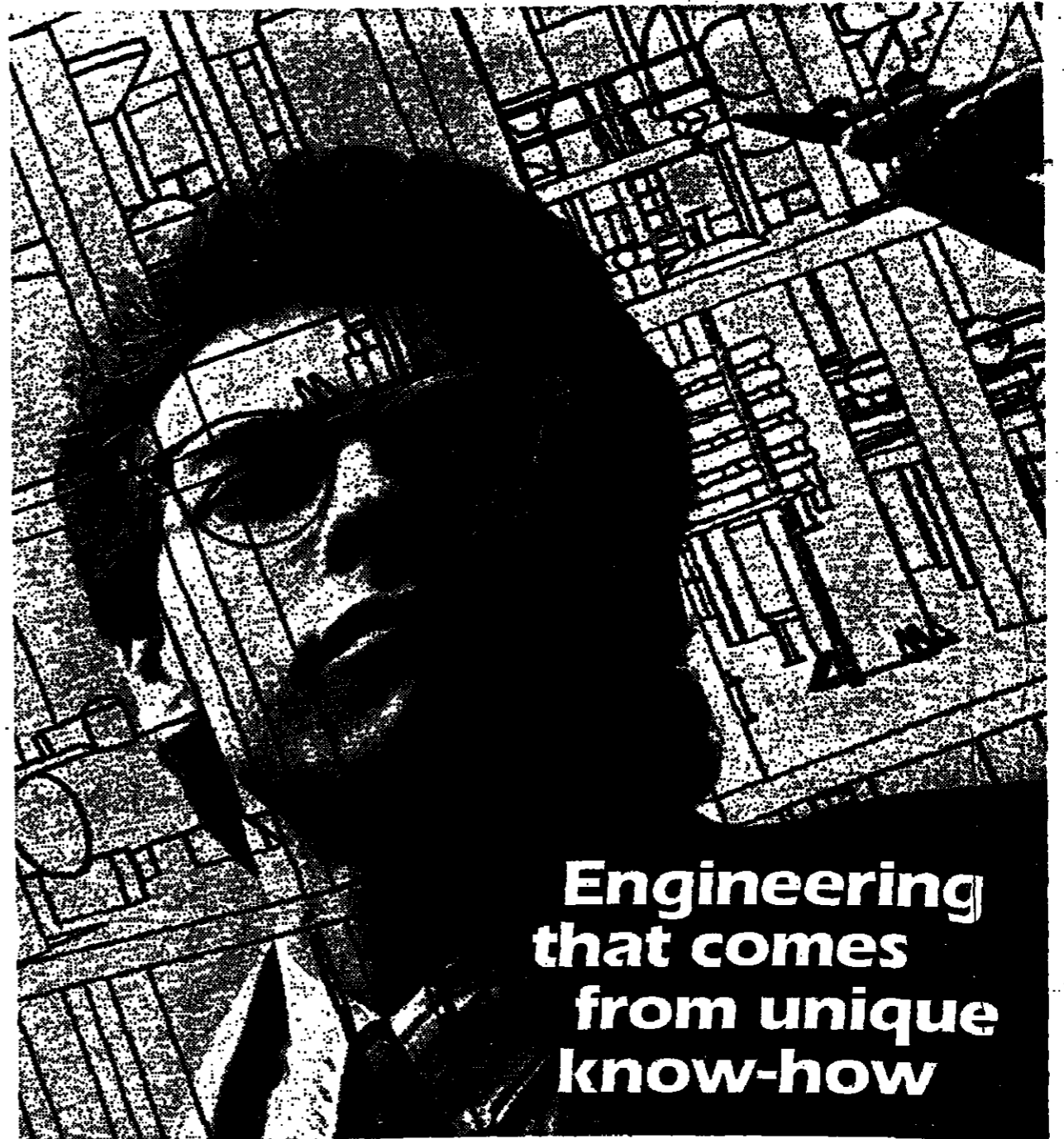
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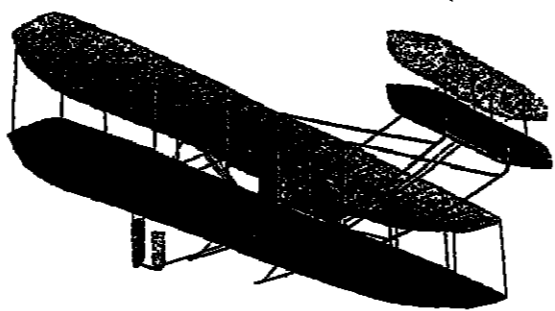
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# 1903. ORVILLE WRIGHT DEFIES GRAVITY. 1989. PORSCHE DEFIES ORVILLE WRIGHT.



On a cold December day in 1903, Orville Wright discovered something that has kept Porsche engineers exercised for years.

Namely, that if you drive into the wind at speed the air rushing towards the vehicle will force it to lift off the ground.

Which is fine if you want to be the first man on earth to experience powered flight.

But annoying if you are obsessed with making what are undoubtedly the world's most revered performance cars.

Naturally, over the years, Porsche engineers have not allowed something as trivial as the elemental forces of nature to deter them.

Indeed, they have produced any number of ingenious ways of ensuring that all Porsches stay well and truly glued to the road.

Although none are as sophisticated as the 'ground-effect' technology on Porsche's 944 S2. Consider, first, the enormity of its task.

Underneath the famous 944 bonnet of the S2 is a brand new engine.

A 3.0-litre, 211 brake horsepower, 16-valve thoroughbred.

Or, to put it in context, it is the most powerful normally-aspirated engine of its type in the world.

Amazingly, the enormous power of the S2 is produced by just four cylinders. Albeit, Porsche-designed cylinders.

Between them, they are perfectly capable of taking the S2 from 0 to 62.5 in 7.1 seconds and to a top speed of 149 mph.\*

Although at Porsche we do not consider speed to be performance.

Balance. Control. Stability. These are the dull words that excite Porsche engineers.

And these are the words that inspired the 'ground-effect' technology on the S2.

This advanced air management system operates in four different areas of the car. The most important being the least obvious.

The underfloor of the S2 incorporates a single smoothed-out panel, allowing the air to flow uninterrupted from the front of the car to the rear.

Meanwhile, the sleek new nose section redirects much of the air that normally finds its way under the car, thus reducing turbulence.

Steering, road holding and braking are all enhanced dramatically as a result.

The rear spoiler deflects air away from the back of the car, which has the effect of reducing lift as the car reaches high speeds.

And not content with one spoiler at the back, the 944 S2 has another, underneath the bumper. As the air flows over it, the downforce adds to the stability of the rear end.

(Autocar & Motor recently heralded the S2 as 'the best handling car in Britain'. Now you know why.)

However, increased control isn't all that's new on the S2.

Every aspect of the car's design has been looked at. Again. And again. And again. (Obsession is a very harsh master.)

The result is a car which has practically been re-designed.

For total stability, the Transaxle drive line system connects the engine to a gearbox in the rear of the car, giving virtually perfect weight distribution of 50% front, 50% rear. (We told you our engineers liked balance.)

Also, the S2 is equipped with a catalytic converter, something it has in common with all Porsche's new models in this country. Indeed, according to a research study carried out by TÜV Bayern of West Germany, the

new 944 S2 has the lowest carbon monoxide emission of any European car.

And naturally, Porsche engineers have made sure that none of the power or performance has been lost.

But perhaps the most remarkable development on the new S2 is the exceptional torque at low revs.

You'll notice it most when you're driving the 944 S2 in town.

Or winding up an Alpine pass (where you will also have the chance to appreciate the S2's new suspension and specially-developed ABS braking system).

Either way, you'll definitely notice it.

Because, as with any function on any Porsche, changes are only made if they make the drive more exhilarating and, ultimately, more satisfying.

'Driving in its purest form', Dr. Porsche called it when he built his first car, the original 356. And no one has come up with a better description yet.

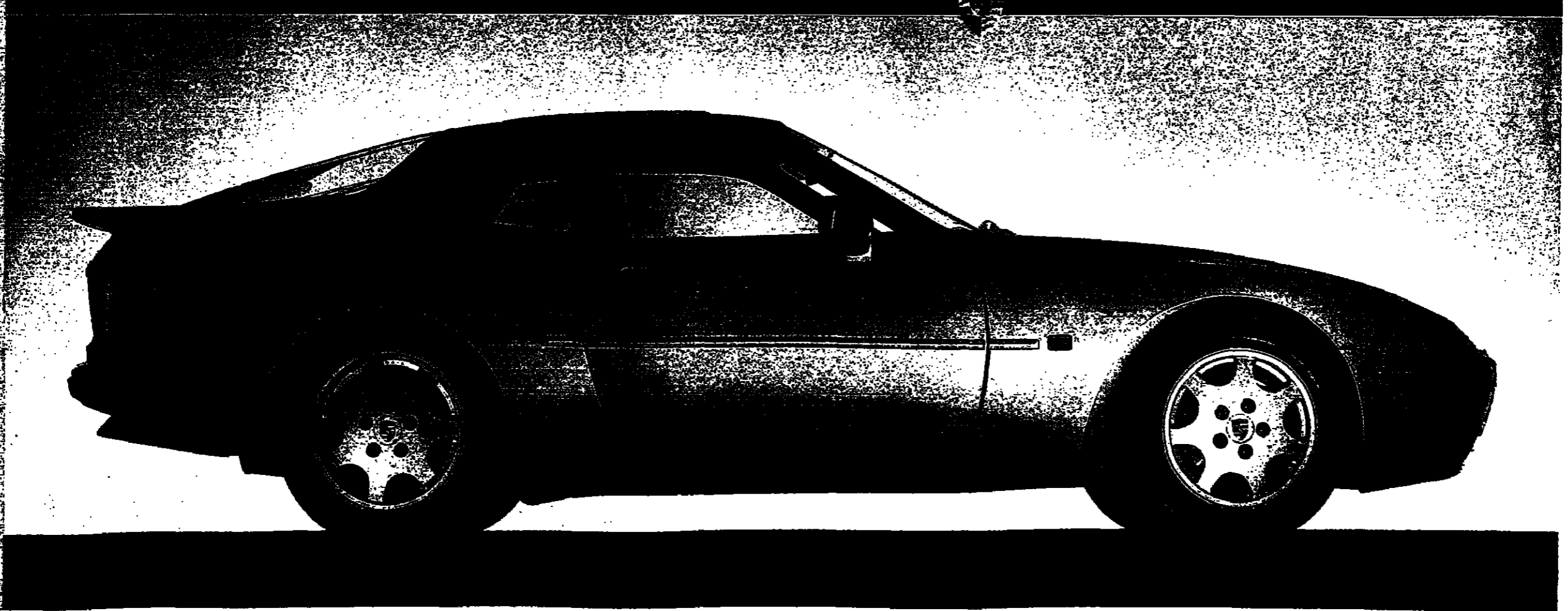
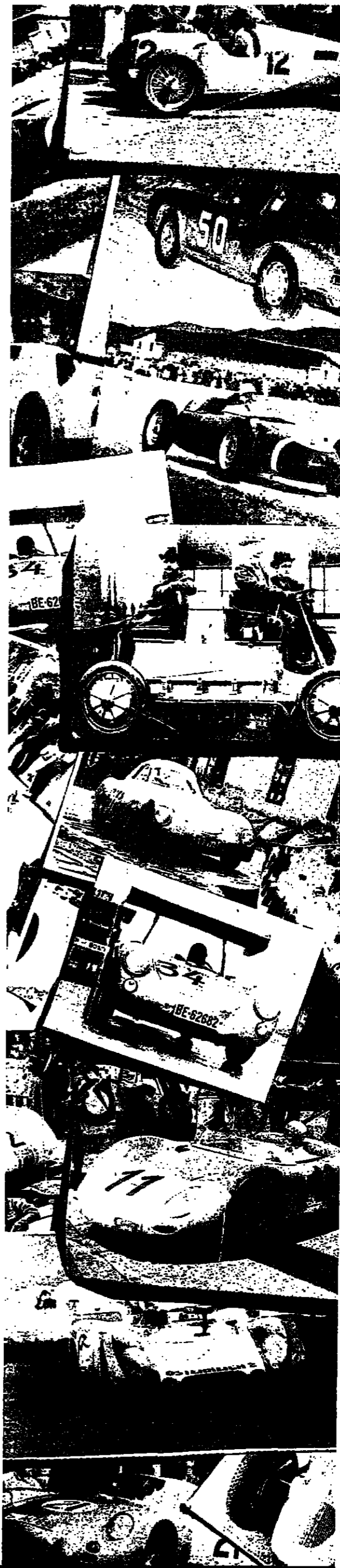
If you would like to know more about the 944 S2 or experience it yourself, contact your local Official Porsche Centre, listed in Yellow Pages, and arrange a test drive.

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Porsche 944 S2 prices start at £32,024 as at 1st September 1989. \*Manufacturer's figures.

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## One of the world's biggest oilfields is 10 years old. Happy birthday!

It is now ten years since the Norwegian-British Statfjord field started producing oil and gas. So far nearly 1,700 million barrels of oil have been produced, and 18,000 million cubic metres of gas have been sold to users in the United Kingdom and the Continent.

The operator for the field is the Norwegian state oil company Statoil. Operator for exploration, development and operations up to 1 January 1987 was Mobil.

Statfjord oil is a light, kerosene-like oil with a low sulphur and metal content. Most refineries use it unmixed, and it yields a full range of good quality, low-sulphur products. Statfjord oil is reckoned as the best of the North sea oil as fuel, and has very good environmental specifications.

Statfjord A, the oldest of the platforms, is a real pioneer in the history of the North Sea oil production. The decision to develop the field was taken in 1974, only a few months after the giant reservoir was proven and while the technology of oil production in the northern part of the North Sea was still in its infancy.

On 24 November 1979 the platform was ready for start-up, after a development that demanded the highest degree of engineering sophistication and practical construction expertise from everyone involved. About 50,000 people from more than 120 Nor-

wegian and foreign companies had a part in the development.

The oil produced from the Statfjord field is tanker-loaded from loading buoys in the open sea. In the early years all the oil was shipped to ports in northwest Europe, but after Statoil built the crude oil terminal at Mongstad in Western Norway, Statfjord oil has a world-wide market.

The gas is transported by pipeline to the Northern Leg Gas Pipeline (NLGP) on the British side, and the Statpipe and Norpipe Gas Transportation systems to Emden in West Germany.

Sales income from oil and gas so far amounts to NOK 300,000 million, or £27,000 million. Half of this is direct revenue for the two countries' exchequers.

It will be many years yet before the Statfjord field is empty. Production prognoses up to year 2010 indicates that another 1,300 million barrels of oil and 55,000 million cubic metres of gas can be produced. Improved oil recovery and alternative use of the installations can lead to prolonged operation of the field.

Statfjord will be a major supplier of oil and gas to the British market for many years to come.

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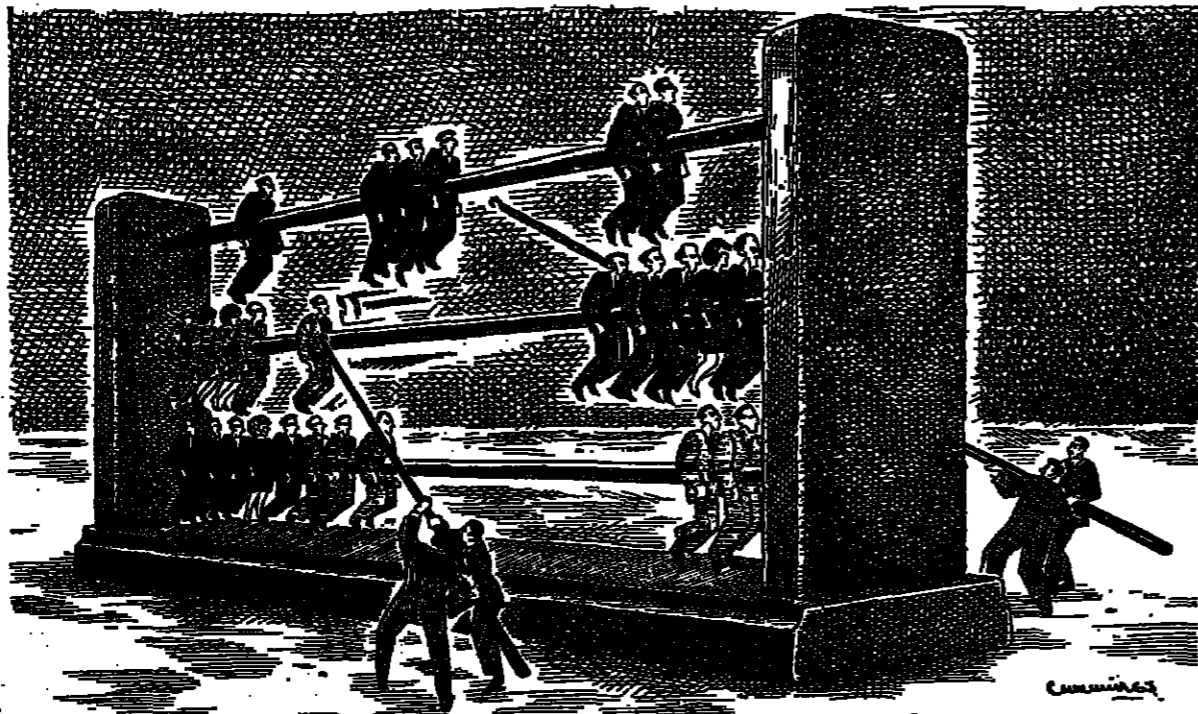


MANAGEMENT

UK accountancy practices

# Partners with a corporate sense of responsibility

David Waller examines how management and ownership are being separated



It is reporting season again for the UK's large accountancy firms. Earlier this month Coopers and Lybrand announced a record 35 per cent increase in its fee income for the 1988-89 year and during this week some of the other big firms are expected to turn in resplendent performances as well.

Growth is not confined to the big firms alone, and is not just a feature of the last financial year. The so-called Big Six have seen their income vault ahead by 20-30 per cent a year for each of the past five years or more, and the medium-sized firms have expanded as well - so much so that they are now the same size as the Big Eight were only a few years ago.

Despite the growth rates, the various markets in which the firms operate - ranging from management consultancy to tax advice and corporate finance - are fiercely competitive. All firms are actively interested in pushing business from their rivals and at all times they are to be found poaching each other's staff.

This combination of rapid growth and fierce competition has posed difficult management challenges for accountancy practices. Those at the top of the firms have found themselves juggling three sets of priorities - the need to expand profitably, the need to impose a central command structure on the business and the need to keep morale and motivation high in what must count as one of the most stressful professions.

These management problems are more pronounced for accountants than they are for other fast-growing businesses. The main difficulty is a structural one: by law, firms of auditors must practise as partnerships rather than incorporated companies. The 1968 Companies Act will change this, but up until now the accountants have had to struggle to find a way of imposing corporate-style management onto a partnership.

The central problem with a partnership is that there is no division between ownership and management. For small firms, that does not present a problem - the firm will hold together through a mixture of shared goals and deference to experienced senior partners. But that cannot apply to the modern firm, the biggest of which have hundreds of employees generating fee income running into hundreds of millions of pounds.

Each and every partner faces unlimited liability for losses sustained or damages brought against any individual partner or the partnership as a whole. The amount of capital he has committed to the firm. The practical consequences of this is that partners may be psychologically unwilling to submit to centralised management authority. After all, if one's entire personal wealth is on the line, there is little incentive for one to relinquish management control over the business for which one is directly responsible. The culture of independence is encouraged by the training which partners have gone through in

order to become chartered accountants.

Hugh Aldous, managing partner of Stoy Hayward, the UK's twelfth largest firm after the latest wave of mega-mergers at the top end of the profession, points out that the formal partnership agreement is often a document of great antiquity, drawn up in an earlier era of the 150 year-old accountancy profession. Typically it would spell out the way in which profits are shared and dictate that one partner be allowed one vote in any matter of consequence for the firm as a whole.

"There is no Companies Act defining management's obligation to shareholders," says Aldous. "If the firm were actually managed according to the detail of the partnership deed, the result would be total and absolute anarchy."

The management problem is to encourage the partners to dispossess themselves of some of their powers in as sensitive a way as possible. Any approach which is manifestly authoritarian could lead to business disaster as valuable human assets pick up their calculators and walk out of the door to join another firm.

Firms have tackled the problem in different ways, but some broad themes emerge:

■ The first step is to devise a strategic plan locating the firm within a well defined sector of the market place. For example, most of what used to be the Big Eight firms have decided to dedicate themselves to serving multinational clients across a range of disciplines. Although many have diversified, this strategy is cited as a reason for this year's wave of mergers between the big firms.

■ By contrast many of the medium-sized firms have abandoned their attempt to serve the big public companies and have decided to address themselves to the "owner managed" business sector, ie companies with a turnover of between £20m and £50m. Robson Rhodes, for one, forged itself a new strategy in 1987 with the help of the Ashridge Management College. As a result of the process the firm committed itself to being "elite, professional and expensive."

■ There must be a restructuring of the partnership agreement - a rebarbering of the constitution of the firm in order to reflect commercial reality. To take one example, the 250

partners in Grant Thornton, the UK's tenth largest firm, voted away significant powers in March this year at their annual meeting. They agreed that the majority required to approve sensitive decisions on the nature of the partnership would fall from 90 to 75 per cent.

They devolved the right to appoint new partners to an elected policy board - although they recognised that in practice partners are actually nominated by a small executive team headed by David McDonnell, the firm's recently appointed national managing partner.

■ The management structure of the firm must be refined. As part and parcel of their reform exercise, Grant Thornton's partners agreed to a radical change in the role of the office managing partner. Hitherto these partners had been appointed by their colleagues in the local offices. Now they are appointed by eight regional managing partners who are themselves appointed by David McDonnell and his executive team. In the past there were no fewer than 25 regional groups.

"This is a huge change of culture," says McDonnell. "In the olden days

the leaders of the local offices were very much local champions. They saw the job as representing the interests of their fellow partners in the office. The job specification has changed significantly. Now the office manager is accountable to the regional management partner who in turn is responsible for implementing firm-wide policies and standards at a local level and ensuring that the offices meet their financial targets.

■ The next step is to tighten up the quality of staff and clients. Deloitte Haskins and Sells, one of the UK's largest firms and now in the throes of a merger with Coopers and Lybrand, went through this process in the wake of its failure to merge with Price Waterhouse in 1984. Since then, says managing partner Alan McFetrich, the firm has shed £5m-£10m of unprofitable turnover and encouraged 70 partners out of a total of 280 to depart. The partnership has expanded by a net ten people to 270 since then, reflecting an infusion of new blood.

Hugh Aldous at Robson Rhodes talks in gleeful terms of a "dross drop" programme. "We went through a computer print-out of all our clients and identified hundreds we didn't want," he says. Five offices have been closed since 1987 and a number of partners have been encouraged to leave.

■ The imposition of financial controls. Venture capitalists which lend to the firms often lament that accountants have no idea how to keep their own books in order. Over the past few years firms have followed their corporate clients and introduced formal budgeting procedures. Performance targets - measured in terms of chargeable hours per person - have been established for each category of employee. Targets have been set for recovering outstanding debts, and cash flow is subject to scrupulous monitoring. Clear chains of financial accountability have been put in place.

■ Many of the firms have recruited finance directors from industry to oversee the tasks, a trend which extends to other disciplines, such as marketing.

■ It is clear that there are problems in the move towards a professionally managed practice, as McDonnell recognises. "The big challenge for the firm is to balance central authority over partners with the need to have motivated entrepreneurial advisers in all our offices," he says. The process for the Big Six firms is easier, he maintains, "because the audit environment encourages deference to the head office."

"The changes have gone through so fast that many partners have seen no impact on their day-to-day business," says David Norton, managing partner of Grant Thornton's Leeds office. "Of course there is scepticism in the provinces."

Accountants will be able to turn themselves into limited companies at the beginning of 1991. By then, many firms will be already be companies in all but name.

## Offering a lease on Soviet trade

Kevin Brown explains why TIP has taken a route through Finland

How do you get started in a country where there is little concept of marketing, property law or enforceable contracts, and where knowledge of western languages is far from widespread? This is the conundrum facing any company wishing to take advantage of perestroika in the Soviet Union, a development which offers the tempting prospect of access to an almost untapped market of more than 280m people.

TIP Europe, the Anglo-Dutch trailer leasing group, has just signed an agreement which offers some pointers:

■ First, it helps to start small, so that the Soviets can get to know you gradually. The TIP deal is for just eight trailers leased for five years, following an earlier agreement to lease five trailers for five years. But TIP is the first western company to crack this particular market, which should be placed to pick up more business later, especially since transport equipment is one of the areas which will have to be modernised rapidly.

■ "This is really just the tip of the iceberg, which is why we are so excited about it," says Tony Rieger, TIP's chief executive, and the company's principal negotiator with the Soviets. ■ Second, work with someone who already knows the Soviet market. TIP made its approach through Finland, where awareness of the Soviet Union is very high, but companies operate in a capitalist environment. The key move was to acquire the leasing interests of Narko, the Finnish trailer manufacturer, which has a long leadership in Finland, and considerable clout with local transport companies dealing regularly with the USSR.

■ Third, remember that the Soviet Union is a federation, that decentralisation is a crucial element of perestroika, and that some of the republics are more progressive than others. TIP entered the market through Estonia, one of the Baltic republics where economic and political change is most advanced, and one of the areas most used to dealing with Finnish companies. The leasing deal was signed with company which is a joint ven-

ture between the local Estonian state-owned transport company and a group of Finnish companies.

Tony Rieger believes Estonia will remain at the cutting edge of economic change in the Soviet Union because of its proximity to the West. "The interesting thing is the rate at which expansion is going on there, and the way people are positioning themselves to take advantage of the geographical and economic opportunities. We are also talking to other companies based in the western Soviet Union, and we think those will be the areas which will benefit most quickly from liberalisation," he says.

But even in Estonia, there are structural difficulties in getting deals signed. "The biggest problem was getting through to the decision makers," says Rieger. "The size of meetings tended to be very large, with technical people, representatives of the various shareholders, translators - all wanting to have their say."

The business languages used were not Russian and English, but Estonian and Finnish. The contracts also presented a major problem because of the lack of a suitable legal mechanism for enforcement in the Soviet Union. In the end, they were drawn up in Russian and Finnish, and are enforceable in Finland. The Finnish link also helped overcome the problem posed by the Soviet Union's unconvertible currency - the deal will be billed in Finnish Marks earned through the joint venture company's activities in Finland.

In the long run, the Soviet Union will have to develop a system of contract law, independent courts and a convertible currency if it is to reap the full benefit of foreign investment, says Rieger. But TIP's experience also presents a tremendous desire for change. "We were cautious because we didn't want to launch into something which was not going to make any money. We didn't want to do something which would mean us providing all the cash and it then going down a black hole. But we did detect a great willingness to find a structure which would be suitable."

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## FINANCIAL HIGHLIGHTS ARAB-MALAYSIAN MERCHANT BANK GROUP

Half Year Ended 30th September, 1989  
Unaudited Consolidated Results

	1989 In Million M\$	1988 In Million M\$	% Change
Net Pretax Profit	34.0	25.0	+36.0
Shareholders' Funds	250.0	213.4	+17.2
Loans & Advances, Net of Provisions	3,215.7	2,563.7	+25.4
Deposits and Borrowings	3,705.9	2,865.2	+29.3
Total Assets	4,727.3	3,581.5	+32.0
Turnover of Money Market Negotiable Instruments	14,511.3	14,581.3	-0.5

Year Ended 31st March, 1989  
Audited Consolidated Results\*

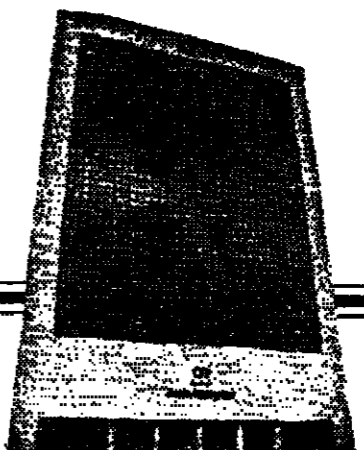
	1989 In Million M\$	1988 In Million M\$	% Change
Net Pretax Profit	58.0	41.9	+38.4
Shareholders' Funds	232.4	201.0	+15.6
Loans & Advances, Net of Provisions	2,750.1	2,321.9	+18.4
Deposits and Borrowings	3,283.8	2,757.7	+19.1
Total Assets	3,987.3	3,306.1	+20.6
Turnover of Money Market Negotiable Instruments	32,895.8	25,299.7	+30.0

- AMMB became the first merchant bank to be listed on The Kuala Lumpur Stock Exchange (The KLSE).
- The Bank was adviser to the first company to be listed on The KLSE Second Board.
- The Bank has set up a property trust management company to manage Arab-Malaysian First Property Trust, the first property trust to be listed on The KLSE.
- The Bank, together with the Nikko Securities Co., Ltd Tokyo and The International Finance Corporation, Washington, launched The Malaysia Growth Fund totalling US\$45.25 million. The US Dollar denominated unit trust is aimed primarily at Japanese investors.
- AMMB became the first Malaysian merchant bank to organise and manage an equity unit trust called Arab-Malaysian First Fund.

TAN SRI DATO' AZMAN HASHIM  
Chairman



\* Subject to Shareholders' approval.



LEGAL COLUMN

Making a mockery of extradition procedures

By Robert Rice, Legal Correspondent

MR LORRAIN Osman, the banker, has been receiving considerable publicity recently for his plight as Britain's longest-serving remand prisoner.

The facts of the Carrion affair, and the collapse in 1983 of the largely fictitious Hong Kong property group with debts of more than £700m are by now well documented.

The Foreign Secretary's order for his return to Hong Kong. Ten days later, he launched his first application for a writ of habeas corpus.

His diplomatic immunity claim was based on three diplomatic notes from the Liberian Embassy to the effect that he had been appointed its special roving ambassador to the EC because of his knowledge of Liberian commercial affairs.

In March, the European Commission of Human Rights rejected a complaint by Mr Osman against the UK. In April, the Liberian Embassy submitted a further diplomatic note "reconfirming" Mr Osman's diplomatic status and protesting at his continued detention.

Other hand, they argue that there is a case for giving him leave so that the matter can be dealt with by the House of Lords once and for all.

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ARTS

ARCHITECTURE

# A cry for Spitalfields

"A cry goes up from the city streets, where wounded men lie groaning." Why did these words from the Book of Job leap into my mind when I contemplated the new proposals that were recently announced for the redevelopment of acres of London to the east of the City? Surprisingly, it is not the sad muddle of London's Docklands that prompted these thoughts but the two major plans that have been prepared for Spitalfields Market and the redevelopment of Bishopsgate Goods Yard and Brick Lane.

Spitalfields is already a name that will have a place in the history of British urban development. It is a paradigm of the problems of planning. Spitalfields borders the eastern edge of the City and edges on the rapidly changing area of Docklands. It has always been home to successive waves of new immigrants. The Great Mosque in Fournier Street encapsulates the history of the neighbourhood in one building: it was built in 1743 as a chapel for the Huguenot silk weavers; from 1809 to 1819 it was occupied by the London Society for Promoting Christianity among the Jews; and from 1819 to 1897 it was a Wesleyan chapel. After the great wave of Jewish immigrants arrived from eastern Europe at the end of the 19th century, the chapel became the Great Synagogue of the Machzikei Hadath Community; and in 1976 it became the mosque for the new arrivals from Bangladesh - Spitalfields now has the highest concentration of Bangladeshis of any city in Britain.

Today the area faces unique pressures. In a new book, *Spitalfields: A Guide for Londoners*, by Charlie Forman (Hilary Shipman, £7.95) the current position is described as though Spitalfields was the new Beirut. "The war for the land is coming from almost all sides. One side is trying to push up from Docklands, another is spread-

ing out from the City, and a third is trying to force a corridor down the Liverpool Street railway line by way of Bishopsgate Goods Yard. Against enormous odds, Spitalfields will end the 1990's with a larger and stronger working-class community living in better housing than it had ten years before. But the enemy has renewed strength, and the odds against Spitalfields in the 1990's are greater than ever." This is an emotive, powerful book written by a man who has seen and tried to tackle the dreadful housing conditions of the area.

It is not possible to look at the redevelopment of this part of London simply as an architectural exercise.

There are two major schemes in the pipeline. In October the Spitalfields Development Group submitted planning applications to the London Borough of Tower Hamlets for revised proposals for comprehensive redevelopment of the 12 acres of land which is largely occupied at present by the Spitalfields fruit, flower and vegetable market. Royal Assent is expected before the end of the year for the Bill to allow traders to move to a new market at Temple Mills.

For any developer, this area offers an incredible opportunity to enhance the eastern fringes of the City. The Spitalfields Development Group is a consortium of Balfour Beatty Developments Ltd, County and District Properties Ltd, and the London and Edinburgh Trust plc. Mr Peter Beckwith of LET plc has great ambitions for his plans. He wrote in December last year to one of his many architects that he felt that the area offers the chance "to produce the very best mixed use scheme in Europe, if not the world."

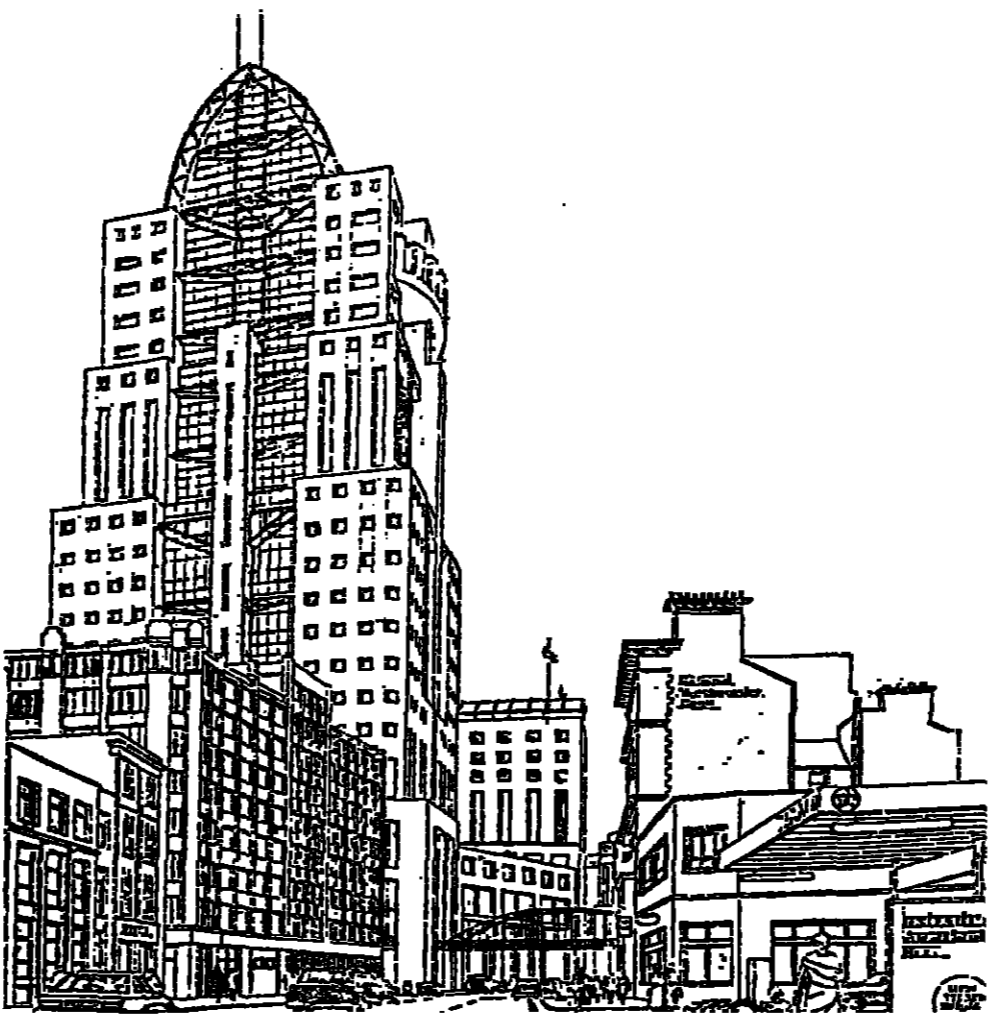
There have been six schemes produced for the site in the past four years. The current comprehensive proposals are

prepared by an American firm of architects, Swanke Hayden Connell, now operating in London; they are best known for the design of the Trump Tower on Fifth Avenue in New York. An earlier scheme, of much more subtlety and ingenuity - but many fewer offices - was prepared by the British practice, MacCormac Jamieson and Prichard, but this has now been abandoned.

The American proposals are for 1.2m sq ft of new building of which 1.1m is proposed to be for commercial use. There will only be 118 "units" of social housing and 35 flats for sale. While Swanke Hayden Connell are the principal architects, the developers have given the fringe housing to more interesting practices: Colquhoun and Miller, Burnell Peasey and Ian Ritchie. A Spanish sculptor/engineer, Santiago Calatrava will advise on the roof vaulting of the shopping Galleria.

Spitalfields demands a more sensitive scheme than this one. It is quite wrong for one firm of very dull commercial architects to design so much of the scheme. Whatever the good intentions of the developers to secure mixed uses, those proposals as they stand are architecturally mediocre. They are a tragic insult to a part of London that offers such an opportunity for a high density redevelopment that should be a real slice of the city.

The second major scheme, a redevelopment of 25 acres around the former Bishopsgate Goods Yard and Truman's Brewery in Brick Lane, is also the responsibility of London and Edinburgh Trust plc - working this time with the British Rail Property Board and Grand Metropolitan plc. The approach here seems much more promising, with something of a pioneering effort to form a partnership with the local community to create an urban village to be



A bizarre new tower that threatens to rise up above the Eastern fringes of the City close to Spitalfields, by architects Covell Matthews Wheatley

developed by a Community Development Trust.

The unhappy element in the scheme is once again the quality of the proposed architecture. The intention to concentrate commercial development, which in theory "pays" for the community benefits, in a giant tower of offices has a crude logic. But it is the design that is so disturbing. Architects Covell Matthews Wheatley have produced a kind of space fantasy to accommodate some

1.2m sq ft of offices. This bizarre looking monster overlooks the "community" development and transport improvements like a terrifying godfather. Is this the only way we can achieve the basic improvements for the entire community?

Both these Spitalfields schemes have undoubtedly tried to balance the commercial and community pressures. You can see how the developers and architects have strug-

gled, but they look as though they are in danger of seriously falling on the architectural front. The architecture betrays all the signs of over development in an area that needs nurture and beauty more than most. The urban and ethnic richness of this part of London has been ignored by the architects, who have designed buildings that belong only in an architectural limbo.

Colin Amery

# Vanek Plays and Adam and Eve

## SONO POLY AND GATE

With barely distinguishable programmes, each prominently advertising the other, two more chips off the old bloc arrive on the London stage - five, if you count Václav Havel's three short Vanek plays as separate entities. Both Havel and the Russian dramatist Mikhail Bulgakov have suffered the slings and arrows of official censorship. But, whereas Bulgakov's *Adam and Eve* had to wait more than half a century for his tatty world premiere at The Gate, Notting Hill, Havel's thumb-nail sketches of Czech conformity, in all its various guises, make their return to London on a tide of fashionable sympathy.

The Vanek of his plays is more a device than a character - a quiet, right-minded conduit for the neuroses and hypocrisies of his countrymen, who has been used by a scattering of Czech playwrights.

The first of Havel's Vanek plays, *Adam and Eve*, written in 1975 for a social gathering at a time when Havel himself had been working in a brewery. It pops up his observations of the working man and relays them through an audience between a peasant and a non-drinking, self-effacing Vanek, a temporary worker under suspicion because he is also a playwright. In the second play, *Prozeste*, Vanek's interlocutor is a cowardly meek man who, entirely and fraudulently argues himself out of signing a petition of protest. The third - and weakest - ridicules the Prague yuppie.

Peter Casterton, founder-director of the Cuneo Theatre Company, has opted for a strongly idiomatic characterisation: the TV tycoon (John Peters) sports designer specs and worn corduroys while the brewery overseer is a belligerent Irishman. Both work well on the stage, although the use of such clearly recognisable characteristics has its problems. The Irishness of Seamus Newham's overseer calls on a cultural awareness which I suspect has more to do with

our attitudes to boozy Irishmen than with Havel's attitude to the working classes.

Tom Knight, as Vanek in all three plays, has the right sort of anonymity - a hint of sympathy for the worker, a hint of scorn for the intellectual, and a hint of embarrassment at the neurotic cozeness of his yuppie friends in *Private View*. The three plays will be presented in rotation, at Sono Poly, two per evening.

The Vanek plays are not vintage Havel, but neither is *Adam and Eve* classic Bulgakov. Written in 1931 and not surprisingly banned by the Russian military, this is a bold, apocalyptic fantasy of science and ideology combined, which the destruction of mankind, *Adam*, an upright young lion of the revolution, and his wife, Eve, a language student, are among a handful of survivors of a gas war which annihilates the rest of civilisation during the first act.

With them is a militarist zealot, a forgetful scientist to whom they owe their survival, a bad novelist, forever eulogising "the fresh pink cheeks of collective peasant women" and a prototype capitalist with a gangrenous foot, who maintains that "as long as two people are left on earth, dollars will have a value."

Far from going forth and multiplying the good children of the revolution, *Adam and Eve* (David Drysdale and Sarah Keyzor) find their positions irreconcilable. He spends his time awaiting news of victory, while she discovers that the poet's revolutionary types are not so obvious and the betrayal of them too amateurish in Stuart Wood's production to stimulate any more than a forensic interest.

Claire Armitstead

# Boulez

## FESTIVAL HALL

Thursday night's BBC Symphony Orchestra concert could easily have come from that golden age when Pierre Boulez was its principal conductor and modernism seemed to stretch in a single unbroken line from Debussy to Stravinsky to Boulez and Stockhausen and beyond. Now we know better, or rather worse. The concert began with Stravinsky's little *Zvezdoliki* and Debussy's *Nocturnes* - scouping suaver now that they were 20 years ago, the textures more integrated, the colours less distinct - and continued with Messiaen and Boulez himself.

*La Ville d'en-haut* is the latest siver of Messiaen to reach London, an eight-minute exchange of piano and strings (Loriod in this performance) and ensemble in which a familiar gallery of bird songs is set against brass chorales and lambent melodies. The intention is the familiar devotional one, but the material endlessly recycled now has lost its freshness and bite.

Boulez's *Le Soleil des eaux* has become relatively familiar in its most recent (1988) and seemingly final revision; sung here by Phyllis Bryn-Julson and the BBC Singers it seemed again a model of concision, intense, gem-like in its total purity and hardness, a vivid response to René Char's texts.

*Le Visage nuptial* has by contrast had a far less chequered history, even by the standards of Boulez's output. It was

begun, again to poems by Char in 1948; a first version was ready by 1951, but not performed until 1967, and then the score disappeared, to be rediscovered in the 1980s when Boulez, set about wholesale revision of his work - the British premiere of the revised version.

It is still an elaborate conception, though the two ondes martenot and quarter-tone writing of the original have disappeared; the soprano and mezzo soloists (Bryn-Julson and the unfailingly impressive Elizabeth Laurence) are enmeshed in a tangle of choral and orchestral lines from which kernels of lyrical expression are allowed to emerge; the chattering activity of the strings in the fourth section "Evadné", and the sensual presentation of the poem in the last are the most striking passages. But despite its misadventures (and for all Boulez's insistence that the central pivotal movement remains fugitive and unwieldy) it carries even now a powerful, knife-edge tension, a sense of a composer straining his creative muscles to the utmost, of pushing such an extreme performer to the limits of their comprehension in the certain knowledge that there are special rewards to be gained there.

Andrew Clements

# Christa Ludwig

## QUEEN ELIZABETH HALL

When Lotte Lehmann was giving her farewell recitals in the 1950s, Christa Ludwig was already embarking on her singing career. Together with Fischer-Dieskau and a handful of others, this mezzo has been one of the enduring giants of the post-war music scene - whose shoulders the tradition of German singing has been borne with dignity and entire reliability. It is remarkable to think that she has probably been active for 35 years or so. At her recital on Thursday the voice was quite unchanged from what we can hear on early recordings. It is still

warm and absolutely steady, but perhaps has a new contour richness in the lowest notes, which she displayed proudly in the low keys she had chosen for the one work on her programme - Schubert's *Die Winterreise*, the cycle which Lehmann once appropriated as her own.

No singer of any musical sensibility could use this work as a vehicle for showmanship, but even so Ludwig is extreme in her refusal to make it entertaining. She simply lets the songs unfold at her own very measured pace and a minimum of verbal inflection and colour-

ing does the rest, with the help of an accompanist, Charles Spencer, in whom she enjoys total accord. This was the winter journey as of some great liner proceeding majestically through frozen waters.

The performance could hardly have provided a greater contrast to that of Brigitte Fassbender, the other female singer in recent years to have taken on what has generally been regarded as a man's cycle. Fassbender is swept away by the songs' most active emotions, of hurt, bitterness and determination. After that it takes time to

adjust to the studied Ludwig, who reflects little of the world's external contact with nature and raw feeling.

For her, as she suggested in her own programme note, this great song cycle is the journey of the inner soul. Her mission is simply to sing it as well as possible and with a heartfelt, deeply serious understanding of the poetry that will communicate to those who are prepared to listen. Many artists have the ambition to sing Schubert this way, but only a few would dare.

Richard Fairman

# Another Bruckner 6th

## BARBICAN HALL

When did we last have two London performances of Bruckner's knotty Sixth Symphony within five weeks? Lolita Zagrock undertook the work with the BBC Symphony last month; and on Thursday the London Symphony showed their pieces in it under Michael Tilson Thomas. Again there was a healthy audience, though perhaps entitled this time by the appearance of Maria Ewing. She is one of nature's Dorabellas (*Così fan tutte*) but it was no mere surprise to find her delivering Fiordiligi's arias than Tilson Thomas expanding Bruckner. Miss Ewing invested "Come

scoglio" and "Per pietà" with scant irony, but much dramatic intensity and commanding volume. Amidst the fearful, scowling Mozart required of his heroine, he basically mezzo voice became several voices; in full cry her effects were riveting, though in pianissimo the vocal colour drained away, for as her delirious challenge of sustaining an unbroken expressive line was unbroken shifted to her histrionic skill, which is formidable. No doubt she could succeed in making a good fist of *Aida* or *Norma* or *Erida*, too, but one still wishes she wouldn't try.

Tilson Thomas had begun the concert with a beautifully balanced account of Bruckner's "Haydn" Variations, neither over-beatly nor too silken, but thoughtfully and warmly sonorous. There were similar virtues in his Bruckner Sixth - speedy, but less hard-pressed than most of Zagrock's substantial and best-realised primary colours: too simple a palette for this involved symphony, and too easily dominated by the (excellent) LSO brass.

Between the clamorous highs and the palpitating lows, whole areas of more complex

feeling were dispatched rather plainly. No single passage came anywhere near Zagrock's subtlety and best-realised insights. Yet, as saving virtues go - they do presuppose something that needs rescuing! - I thought Tilson Thomas's grasp of Bruckner's symphonic profile and broad proportions quite admirable, and quite satisfying as far as it went. Any early prospect of a Tilson Thomas Eighth or Ninth, however, would strike the heart with a same dismaying thud as a Ewing Isolda: please, not yet.

David Murray

# Felicity Lott

## WIGMORE HALL

It is a special honour for an English singer to be accepted as an interpreter of French music across the Channel and Felicity Lott is one of the few artists to have been accorded such recognition in recent years.

Both in operatic appearances in Paris and Brussels and in recitals, she has been welcomed as a valued guest. It helps that she graduated in French journals usually pay respect to her accomplishment in the language, even if they cannot help pointing out that a native French speaker would get more out of the words.

The balance is a fine one and it was reflected in the recital that the singer gave with Graham Johnson at the Wigmore Hall on Saturday, featuring an all-French programme with favourite songs by Fauré, Bizet and Debussy.

Apologies were made at the outset that singer and pianist both had had colds. But there was little to show in the singing, other than perhaps a shortage of firm tone lower down.

This was "Flott" as lambent of voice as ever, shaping Fauré's "Joy" and Debussy's "C'est l'exotisme" with a sensuous silkiness of line.

She is fortunate, too, that in Johnson she has an accompanist who will provide the discipline (no rallentandos!) this music needs.

What was lacking was any deeper interpretative impulse. With the exception of a small group of songs by Roussel, where the singer got to grips more actively with the words, one composer sounded much like another, each song as ravishingly beautiful as the one on either side.

Contrary to popular belief, there is scope for more in a programme of French *mélodies*, as one can find by sampling almost any recital disc by Gérard Souzay or Pierre Bernac.

This was not, however, the occasion for sounding ungrateful.

The audience had been given a full programme, when it might have had none at all, and enough vocal beauty to fill half a dozen recitals by most other performers.

The give away is that guitarist Billy Duffy actually dares to play solos, and very good they are, too. The Cult has a discipline and ability to flesh out the music which is rare in a genre where image and noise is all. The mix of total rock out with fairly discernible melodies makes the Cult a band you can sing along to as well as shake along to.

And Astbury, while on the beefy side, obviously pulls in the girls, who were present in numbers quite out of order for a regular heavy metal bash among the lads.

By the time the Cult got down to their anthem, and, let's face it, pop chart hit, "She sells sanctuary" (Wembley much improved these days) it was usual stomping, fist-clenching, body bending, brain blown, self.

Band and fans had very happily, individually and severally, got off, and it was time to fade away.

Antony Thorncroft

**BUILDING MATERIALS AND AGGREGATES**

The Financial Times proposes to publish a Survey on the above on

**13th February 1990**

For a full editorial synopsis and advertisement details, please contact:

**ALISON BARNARD**

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Number One, Southwark Bridge London SE1 9HL.

**FINANCIAL TIMES**  
LONDON'S BUSINESS NEWSPAPER

# ARTS GUIDE

November 24-30

- MUSIC**
- London**
- The London Philharmonic conducted by Sir Georg Solti. Shostakovich, Tchaikovsky. Royal Festival Hall (Thurs) (928 8800).
- Vienna Philharmonic Orchestra** conducted by André Previn. Haydn, Strauss, Dvorak. Royal Festival Hall (Thurs) (928 8800).
- Paris**
- Quatuor Sak. Schumann, Gageax, Dvorak (Mon). Salle Gaveaux (45832030).
- Orchestre Colonne conducted by Carla Maria Tarditi with the Colonne Orchestra's choir, Ariey Becce, soloist. Berlioz, Rousset, Franck (Mon). Salle Pleyel (45832072).
- Dimitri Bashkirtov, piano. Schubert, Liszt, Brahms (Tue). Salle Gaveaux (45832030).
- Orchestre de Paris conducted by Kent Nagano, with Nobuko Imai. Debussy, Takemitsu, Bartok (Wed, Thurs). Salle Pleyel (45832072).
- Barry Douglas, piano. Beethoven, Shostakovich, Berg, Liszt (Thurs). Salle Gaveaux (45832030).
- Amsterdam**
- Cleo Laine and John Dankworth with the Metropole Orchestra. Concertgebouw (Tues) (718 945).
- Milan**
- Amadeus Piano Trio: Norbert Brainin, (violin), Martin Lovett, (cello) and Arnaldo Cohen, (piano). Mozart, Beethoven and Brahms (Wed) (7601755). Conservatorio G. Verdi.
- Rome**
- Michael's Reiser: Chamber version of Second Act of Karlheinz Stockhausen's opera *Demersung aus Licht*, conducted by the composer (Wed). Teatro Olimpico (383304).
- Frankfurt**
- Frankfurt Radio Orchestra conducted by Raymond Leppard. Britten, Schumann and Sibelius (Thurs). Alts Oper.
- Vienna**
- Wiener Streichensemble conducted by Marie-Louise Oechsle. Stravinsky, Bach, Schoenberg (Mon).
- Wiener Schubert Trio. Mozart, Schumann, Musikverein (Tues).
- Hans Kamm, piano, plays Mozart at the Konzerthaus. (Wed).
- Andrei Cavrilov, piano, Schumann, Schubert, Musikverein. (Thurs).
- Madrid**
- Die Deutschen Bach-Vocalisten and the Collegium Aureum, conducted by Gerhard Weinberger. Bach (Thurs). Auditorio Nacional de Música (337 01 00).
- New York**
- New York Philharmonic, conducted by Zubin Mehta, with Fiona Simon, Yoko Takeya, Charles Rex (violins) and Warren Deck (truba). Vivaldi, Nielsen, Kellaway, Nielsen (Tue), and conducted by Giuseppe Sinopoli, with Bruno Ceccobello, Ravel, Mussorgsky-Ravel (Thurs). Avery Fisher Hall (874 6770).
- Shanghai Quartet. Haydn, Shostakovich, Beethoven (Thurs). Alice Tully Hall Lincoln Center (874 6770).
- Washington**
- Academy of St Martins in the Fields conducted by Sir Neville Martinson. Berlioz, Strauss, Copland, Schumann (Wed). Kennedy Center Concert Hall (467 4500).
- National Symphony Orchestra** conducted by Gary Bertini with Rudolf Buchbinder (piano). Beethoven, Berlioz (Thurs). Kennedy Center Concert Hall (467 4500).
- Chicago**
- Chicago Symphony Orchestra conducted by Neeme Järvi. Part, Scriabin, Mussorgsky (Tue), and conducted by Gennady Rozdhevitsky. Shostakovich, Prokofiev, Stravinsky (Thurs). Orchestra Hall (435 6666).
- Tokyo**
- Prague Symphony Orchestra conducted by Jiri Belohlavek. Schubert, Tchaikovsky. Suntory Hall (Mon, Tues) (561 5012, 534 7207).
- I Musici. Albinoni, Vivaldi, Gloriana (Wed), Vivaldi (Thurs). Bunkamura, Orchard Hall (458 8111).
- Tatiana Shebanova (piano). Beethoven, Chopin, Satie. Tokyo Bunka Kaikan (Wed) (265 6361).
- Leipzig Gewandhaus Orchestra conducted by Kurt Masur, with Annette Schmitt (piano). Beethoven. Suntory Hall (Thurs) (505 1010).
- Traditional Japanese Music. Shakuhachi (bamboo flute) solos. ABC Hall, Shiba Koen (Thurs) (436 0430).

# The Cult

## WEMBLEY ARENA

What makes the Cult different from a myriad other heavy metal thrash bands?

Their hair is regulatory length - not too long, not too short, shaken to totally hide pallid complexions; their lead singer Ian Astbury spits and swears with precision, constantly checks his crutch to ensure that he's all there, and spends the requisite amount of time on his knees making love to the mike stand; the guitar and bass players wander aimlessly around the stage like inquisitive lion cubs, pausing occasionally to rub backs; the clothes are leather; the lighting dazzles; and the music is loud enough to ensure an early deafness allowance.

What's the sizzle that packed Wembley for two nights over the week end?

The attraction of the Cult is that they are basically a pop band born at the wrong time. A decade ago any hopeful young provincial musician was indoctrinated into punk. Then the progression was usually into some form of heavy metal. The Cult took the Gothic route, wrapping their music around Tolkien mythology.

Slowly they are returning to the real world and in a couple of years time they will probably discard the red Iron Cross that still decorates the drum kit and become an out and out rock group.

For the moment, though,

they have achieved the dream of all record industry moguls - a cross over band that appeals to many market segments.

Astbury has already mastered the line "Are you ready for a little rock and roll?" and then the Cult is off and playing the mainstream pop music of two decades.

The give away is that guitarist Billy Duffy actually dares to play solos, and very good they are, too. The Cult has a discipline and ability to flesh out the music which is rare in a genre where image and noise is all. The mix of total rock out with fairly discernible melodies makes the Cult a band you can sing along to as well as shake along to.

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Antony Thorncroft

# FINANCIAL TIMES

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Monday November 27 1989

## All together, now

THE SCENES in Prague over the weekend are ones that Europe has been waiting for the last 21 years.

Of all the countries subjected by Soviet power after the Second World War, Czechoslovakia was closest to the heart of Europe, literally and figuratively. Sacrificed to Hitler by the western powers in 1938, it was in 1945 spontaneously and genuinely pro-Soviet. But in 1948 Stalin insisted on its subjection to the same monolithic and brutal version of communist rule as the rest of eastern Europe. At the time, his Czech followers faithfully implemented his instructions, though many soon found themselves among the victims. But the Party retained enough life in it to be able, in 1988, to reflect society's desire for change.

Just how far that change would have gone in the direction of full multi-party democracy we shall never know, but in the climate of those times Czechoslovakia would probably have remained in some sense socialist, and the reforming Communists might well have retained power even in a free vote. In any case, the country's external alignment with the Soviet Union was never questioned. The suppression of the "Prague Spring" by Soviet tanks was thus all the more offensive for being a gratuitous attack on Czechoslovakia as a whole, including its Communist Party, which had afterwards to be purged from top to bottom. The resulting regime has governed Czechoslovakia for 20 years without a shred of legitimacy even by communist standards, and no semblance of popular support.

### Unstoppable momentum

Now at last it is ending. The events of the last few days follow a pattern now happily familiar, and clearly reflect an unstoppable momentum. In Czechoslovakia as in East Germany, the opposition is not yet organised, and the problems of economic restructuring are formidable to say the least. But a Peking-style "Tiananmen Square solution" can now be ruled out, and there is no other way the situation can be stabilised except by conceding free elections to the east. The reformers are ready to accept this, and Mr Alexander Dubcek, the reforming Communist leader of 1968, is a heartening symbol and he might be an appropriate head of state in the new regime. Whether today's Czechs and Slovaks are still ready to support "socialism" with a human face, is much more doubtful. The choice, in any case, must be for them alone to make.

A process of sweeping political change is now under way in all five of the genuine Soviet satellite states of eastern Europe (the Romanian dictator having shrewdly extracted himself from that status, with western encouragement, back in the 1960s). There must be some safety in these numbers. Whatever pitfalls lie ahead for Mr Gorbachev at home, the likelihood of any Soviet leadership using military force to overthrow five east European governments is surely remote.

### Warsaw Pact

Even more so, now, is the prospect of a Warsaw Pact offensive against western Europe. That is a political reality of which the US, struggling to reduce its budget deficit without increasing taxation, is bound to take account. But Nato still exists, and must remain in existence at least until the new politico-military shape of eastern Europe and the Soviet Union is fully clear. That will be some time yet, and during that time Nato's members must continue to behave like good allies, reducing their forces only by agreement and in response to changes on the other side, whether these are negotiated or unilateral.

The process of political change in eastern Europe can be more safely managed if the Warsaw Pact too remains in existence, with its present membership if not its present structure, during this transitional period. That implies keeping the two German states separate for the same period, since one state could hardly belong to both alliances. But that in turn is a reason why the period should clearly be understood to be transitional, since in the last resort the people of each European state (and in particular the people of East Germany) must be free to decide which alliance, if any, it wishes to belong to.

Meanwhile, the prospect of reforming governments throughout eastern Europe opens the way to real economic co-operation among them. Western aid, which must remain conditional on genuine political and economic reforms, now has the chance to act as a catalyst of change, with unity overcoming the dangers of resurgent nationalism, just as Marshall Aid did for west European unity in the late 1940s. All Europeans, east and west, should get together as soon as possible to work out ways of promoting the causes of freedom in Romania, and Albania, since those two European peoples are now the only ones prevented from speaking for themselves.

## India votes for change

THE INDIAN electorate, half a billion strong in the world's largest democracy, has voted for change and against corruption.

The general election appears to leave all parties short of a working majority. But the voters' message has been unmistakably clear: it expects politicians, in return for the power vested in them, to remain honest and to root out the corruption which is in danger of becoming endemic at all levels of official Indian life.

That was the message in 1984. Mr Rajiv Gandhi was swept to power with a landslide victory, partly on a wave of sympathy following the assassination of his father, Mrs Indira Gandhi, by Sikh extremists, but mainly because of his convincing claim that he would fulfil the role of Mr Clean Government corruption, principally the Bofors arms scandal, has sullied that image.

### Congress

It is for this reason that Mr Gandhi and his Congress Party have not fared as badly as they feared, although they have suffered the humiliating loss of about half their support since 1984. Congress was the opposition party in most southern state governments and therefore benefited as the voters rejected the parties in power. In the electorally more important north, the reverse was the case and Congress has suffered badly.

The new Mr Clean is Mr V.P. Singh, a modest man whose integrity remains unquestioned. He was a former close ally of Mr Gandhi and served as an exceptionally able

finance minister. He quit the Cabinet and went into opposition because of high-level government corruption.

The success of his National front coalition of five parties, while a personal triumph, probably the most complicated possible result for India: a hung parliament. Mr Gandhi would appear to have little chance of forming a government as minority party support is unlikely. But Mr Singh would need external help to secure an overall majority. The obvious choices are the Bharatiya Janata Party, a right-wing Hindu fundamentalist party, and the Marxist Communist Party of India. Each has done well in the poll and insists it will not serve with the other in a coalition government.

### Horse trading

Clearly there is much horse trading to be done once the final results are known. If, for example, Congress were to split, with some factions joining Mr Singh, the chances of a broad moderate coalition government would be enhanced. Mr Gandhi's personal position will not become clear for some time. He seems temperamentally unsuited to opposition and his party may prove unforgiving if Congress is not involved in government.

Whatever happens, democracy has proved itself again in India. In spite of the violence and ballot rigging, both of which have reached disgraceful levels, the majority of Indians have abided by the rules and then used their ballots to change the balances of power. They may have ended the Gandhi dynasty's hold on government and with it the cult of the individual which has plagued Indian politics for decades. The fact that difficult compromises will now be needed to form a new government is by no means the worst outcome for Indian democracy.

Mr Charles Keating was unusually reticent last week when he appeared on Capitol Hill. He was due to testify to the House Banking Committee about the collapse of his Lincoln Savings and Loan mortgage and property lending group at a cost to US taxpayers of \$2bn (£1.25bn) to \$2.5bn. But he refused to answer questions, invoking his constitutional Fifth Amendment rights against self-incrimination, as well as his right not to be photographed or broadcast.

Mr Keating faces a battery of legal actions and inquiries, including a \$1.1bn racketeering and fraud suit. In the past, however, Mr Keating has been more voluble. He has boasted of his high-placed friends and contacts. He was appointed by President Nixon to an anti-pornography commission; was the final campaign manager for former Treasury Secretary John Connally's disastrous presidential bid; employed current Federal Reserve chairman Alan Greenspan as a consultant; met White House Chief of Staff Donald Regan to urge the appointment of an associate to the main savings and loan regulatory board; and, most significant of all, donated or raised nearly \$1.4m for five US senators.

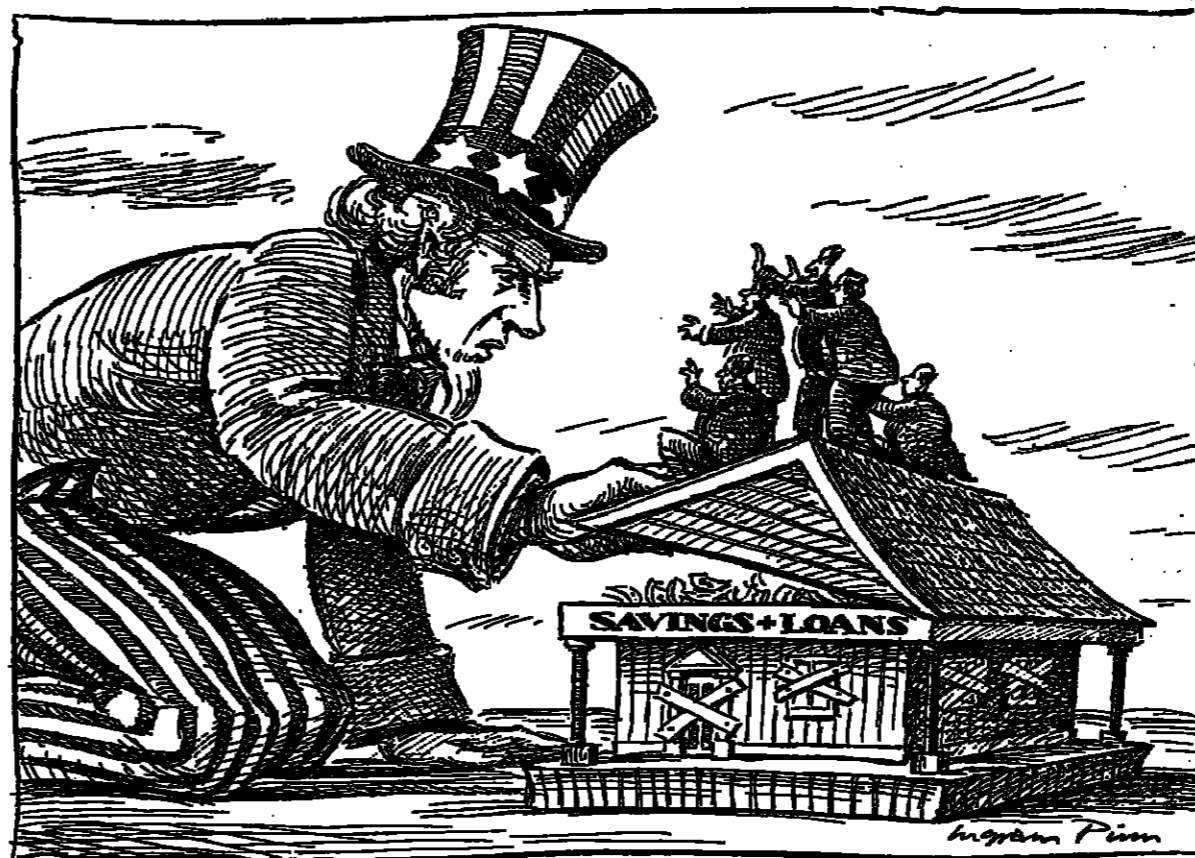
Earlier this year, Mr Keating said that when asked whether his political support in any way influenced several political figures to take up my cause, I want to say in the most forceful way I can: I certainly hope so.

The Lincoln saga is only part of the much larger story of the collapse and rescue of much of the savings and loans industry, which officially put at \$164bn, but more likely to be \$250bn to \$300bn. Lincoln has become a national scandal because it has lifted the veil on the mutual dependence between businessmen and politicians - the search of the former for access and influence and the need of the latter for large sums of money for election campaigns, and especially television advertising spots. Senators now have to raise an average of \$12,000 a week for their six-yearly re-election campaigns.

Savings and loans - known as thrifts - occupied the same role as building societies in Britain in financing house purchase by raising small-scale deposits. But there were two key differences. First, savings and loans have independent shareholders like ordinary companies, rather than being depositor-owned, as they have been in Britain. This allowed takeovers by operators such as Mr Keating. Second, much of the thrifts' lending was on long-term fixed interest mortgages. While there was also a limit on the interest paid on deposits, savings and loans were increasingly handicapped during the 1970s by the rise in interest rates. So in 1980 the cap on interest paid on deposits was lifted, and in 1982 savings and loans were allowed to diversify away from low yielding mortgages into direct investments such as property developments and land, as well as high return junk bonds.

This led to an extraordinary period in the early-to-mid 1980s as a wide variety of businessmen brought up savings and loans and expanded them rapidly, notably in Texas and California. On the deposit side, brokers put together packages of up to the \$100,000 limit of Federal deposit insurance - an open-ended scheme which was inadequately funded and, with lax regulation, provided no discipline. On the asset side, the new owners became active in risky property developments and junk bonds.

Mr Keating was at home in this world. He had a chequered history, having signed a consent decree with the Securities and Exchange Commission in 1979 (admitting, nor denying liability) over an alleged fraud. This background did not prevent him, as it would now, from buying Lincoln in 1984. He expanded its operations into currency futures, junk



Peter Riddell looks at a banking scandal which has turned into a big political issue

# Lifting the veil on dependence

bonds, large areas of undeveloped land and property developments. Mr Keating soon had problems with regulators, particularly in San Francisco, suspected Lincoln of being \$800m over the direct investment limit and of lending without proper appraisals. In spring 1987, Lincoln not only used the regulators but also mobilised the recipients of his campaign contributions.

Mr Keating tried, and failed, to seek exemption from this change - including commissioning Mr Alan Greenspan, then an economic consultant, to produce a report in early 1985 on the case for higher direct investment. Mr Greenspan's report praised Lincoln's management as "seasoned and expert" with "a record of outstanding success." Mr Greenspan, now Fed chairman, has expressed surprise and regret at what has since happened.

Throughout this period Mr Keating built up political contacts - disbursing money to a wide variety of local and national politicians. But the bulk went to the five US senators listed in the table. These were not just arm's length donations; Mr Keating travelled with them together to the Bahamas with their Representative (and now Senator) John McCain from his main base of Arizona. Mr McCain has subsequently repaid the cost of the airfares. Mr Keating also organised a large fund-raising event in 1987 for Senator Donald Riegle of Michigan, since last January the chairman of the Senate Banking Committee.

Mr Keating and his associates raised big sums for Democratic Senators John Glenn of Ohio (the former astronaut), Alan Cranston of California and Dennis DeConcini of Arizona. Either Lincoln or Mr Keating had a connection with their states. Political friends in the right places

became increasingly important as he came under closer scrutiny. Regulators, particularly in San Francisco, suspected Lincoln of being \$800m over the direct investment limit and of lending without proper appraisals. In spring 1987, Lincoln not only used the regulators but also mobilised the recipients of his campaign contributions.

### The five Senators

(Contributions made directly or raised by Keating and associates)

Dennis DeConcini (Dem, Ariz): received \$48,000; later said he would return the money.
Alan Cranston (Dem, Cal): received \$39,000 directly, plus \$850,000 for political groups controlled by him and \$65,000 for California Democrats.
John Glenn (Dem, Ohio): received \$34,000 in campaign contributions; an action committee associated with him received \$200,000.
John McCain (Rep, Ariz): received \$112,000 directly; has paid back \$13,400 for flights to Bahamas with his family.
Donald Riegle (Dem, Mich): received \$76,000, later returned.

On April 2 and 3, 1987, there were two meetings with the regulators in the office of Senator DeConcini. Senator Riegle did not attend the first, the second included all five. At the first, Mr Gray of the Federal Home Loan Bank Board alleges that a relaxation of the direct investment rule for Lincoln was demanded. He says the sena-

tors tried "to subvert the regulatory process for their wealthy friend and contributor." The senators insist they were only seeking information on why the Lincoln inquiry by the regulators was taking so long. At the second meeting, Senator DeConcini allegedly outlined Lincoln's proposals for resolving the problem, while regulators from San Francisco described the thrift as a "ticking time bomb." Senators McCain and Glenn were then recorded as saying they wanted no special favours.

Despite these appeals, the San Francisco regulators pressed for Mr Keating to be removed and for Lincoln to be taken over. However, the board's head office in Washington was reluctant to take such a drastic move, arguing that the local regulators had not made out a sufficient case. After further reviews under Mr Danny Wall, who replaced Mr Gray as chairman, no direct action against Lincoln was taken. Indeed, after considerable friction with San Francisco, the Washington head office acquired responsibility for Lincoln in May 1988. It was only last April that Lincoln was taken over with large losses on risky investments, as well as allegations that money (possibly up to \$100m) was illegally taken out of Lincoln by Mr Keating and his associates.

There is a further twist to the story. The Securities and Exchange Commission also became interested in the activities of American Continental, Lincoln's parent, but found his inquiries hampered not only by Mr Keating but also by the accountancy firm Arthur Young (now merged into Ernst and Young). Mr Richard Breen, the chairman of the SEC, has

claimed that Arthur Young had been "very unhelpful, very uncooperative and very unco-operative in any shape, way or form."

Another accountancy firm brought in by the regulators claims that Arthur Young approved accounts which substantially overstated profits, possibly by up to \$135m. Arthur Young, which parted from Lincoln in October 1988, denies these charges. Mr Jack Atchison, the Arthur Young partner responsible for the audits, joined American Continental in early 1988 at a salary of over \$80,000. He has refused to testify before the House Banking Committee.

The overall impact of these delays, whatever their cause, between spring 1987 and the Federal takeover last April is estimated to have added \$1bn to the cost of the rescue. In this period American Continental also sold \$200m of now almost worthless bonds (not protected by Federal insurance) via Lincoln outlets. The blame for the slow response lies in a combination of finding and inadequacies by the regulators, reinforced by the refusal of top levels of the administration or Congress to take an interest in Lincoln's increasingly obvious problems. The actions of the five senators in April 1987, and of Senator DeConcini subsequently in talks with the regulators, reinforced, rather than created, these mistakes.

The collapse of Lincoln, and subsequent revelations of the role of the five Senators and of the regulators, is now a big political issue. Over the past six weeks a series of charges have been made, including the regulators, reinforced by the refusal of top levels of the administration or Congress to take an interest in Lincoln's increasingly obvious problems. The actions of the five senators in April 1987, and of Senator DeConcini subsequently in talks with the regulators, reinforced, rather than created, these mistakes.

The five senators have captured the headlines because of their number and their prominence. All have denied wrongdoing, claiming they were merely performing a service for a constituent (albeit in several different states). The Senate Ethics Committee has appointed independent counsel to see whether there are grounds for further inquiry.

But whether or not the senators have broken the Senate's rules is almost beside the point. The significant question is that the meetings took place at all and were regarded as normal by the senators. Money may not buy decisions, but it does buy access to legislators, and thus to regulators.

This mix of money and politics is also reflected in the president's use of ambassadorships to reward large campaign donors with no foreign experience. Similarly, there have been allegations that low income housing programmes were exploited during the Reagan era to benefit prominent Republicans and donors.

The affair of Mr Keating and the five Senators may just be a footnote in the whole sorry savings and loans saga, but it could also be a spur to reform of the campaign finance laws to limit special interest contributions which Congressional leaders plan to push next year. A favourite Washington saying is that what is wrong with American politics is not what is illegal but what is regarded as legal and normal.

## Japanese in Brussels

To Belgium at the weekend to learn about the Japanese art. There is a collection of exhibitions all over the country with much of the best of what the Japanese have to offer, and the Belgians are flocking in. On Saturday afternoon (with the exception of those queuing for the exhibition on Japanese Buddhism).

The overall title is Europa 88: Japan in Belgium. Europa is a mixture of Europe, obviously, and *opelle*, the Latin term for the harvest festival. The Belgians have been putting on these shows every two years or so since 1969 when they started with Italy. The idea is that you invite another country to send its treasures to Belgium around three months and the local population absorbs them in increasing numbers. There were over 1.6m visitors to the exhibitions on Austria two years ago.

Japan was the breakthrough. Hitherto, all the exhibiting countries had been European. The Japanese agreed to come not because of Belgium, but because of Brussels, which is a kind of magic word to them. That is where a lot of them think that power lies in Europe. Out of total costs of around ¥1bn, the Japanese Government put up around two-thirds. There were also subsidies from companies such as Honda, which has a large distributing base in Belgium.

### Stick to golf

The General Commissioner responsible for getting the Japanese programme under way is Jacques Grootbaert, a former diplomat who has been chairman of Générale de Banque since 1980. Grootbaert was Ambassador in China and was one of the last Westerners to talk to Mao Zedong before he died. He says that Mao could hardly speak, but insisted on

## OBSERVER

going through all the formalities of receiving foreign emissaries.

The Chinese rather liked Grootbaert and were always inviting him. This year, however, he was invited to his posts on Sino-Belgian and Sino-European organisations as soon as the troops went into Tiananmen Square. Anyway, it was for his Asian knowledge, as well as for his many other international contacts, that he was given the Japan show. He says he found the Japanese quite difficult to persuade at first. It was largely the Brussels tag that did it. Also, the Japanese only wanted to send classical works - not modern or controversial - and they wanted the pieces back as soon as possible. The Buddhist exhibitions could run much longer, Grootbaert claims. If the Japanese would let them.

Grootbaert was also warned not to expect the Japanese in Europe to come to the exhibitions. When the Japanese abroad are not working, they play golf, he was told. And that seems to be true. Some Belgians take great pride in attracting the Japanese colony in Düsseldorf to Belgian rather than German golf courses at weekends, though a sizeable number of Japanese did turn up at the Enkaku puppet theatre at the Théâtre National, followed by a saki party, on Saturday evening.

### Video art

As it happens, some of the modern work which the Belgians did manage to secure is immensely impressive. There is a young artist called Yasumasa Morimura on show in Gent who is plainly fascinated by western influences - the Impressionists, van Gogh, modern Americans, the lot. He tends to take a

## British past

There was a British Europa in Belgium 1973 - the year Britain joined the European Community - and some grand exhibitions. Some held in: Lord Drogheda, Sir Charles Villiers, Sir Francis Sandlands and Lord Stokes. Sir John Bethel, the British Ambassador to Belgium, wrote that it was "the largest single British cultural event ever mounted outside the UK".

I looked back at the programme and was impressed by the range: an evening with Sir John Betjeman, the Laureate, and another evening of French poetry. Lord Arman lectured in French on the British University System and Sir Frederick Dainton, the chairman of the University Grants Committee, also in French, on Science and Society.

A very special British show was called For a Total Environment - "A major exhibition covering the vital problems of clean air, water, the transformation of mining regions and the preservation of historic buildings." It was arranged by the Department of the Environment. Those were the days when Britain was ahead of the times.

### Columbus next

The next Europa in 1991 will feature Portugal. That is not quite such a tame idea as it sounds after Japan. The year 1992 will contain a notable 500th anniversary - Columbus's discovery of America. The Belgians have secured Portuguese support for getting in with the first of the major

exhibitions. After that, the aim is the Soviet Union, although the arrangements are still tentative.

### British past

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### No joke

Sadly, there do not appear any jokes in Belgium any more, at least outside the European Commission, which was closed. The Belgians go about their business, looking very prosperous, on the way to overcoming their linguistic problems, and visiting exhibitions. In some parts of the country they even have access to 25 different television channels. Even Mrs Thatcher was shocked to hear that when told by the Belgian Ambassador. So today there is, I am afraid, no tallpice.

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ECONOMIC VIEWPOINT

# Look at sterling, not trade figures

By Samuel Brittan

One of the silliest canards being down is that it would be sensible to repeat next year the British policy mix of 1981, when an unexpectedly tight Budget in a recession, which led to the famous protest by 364 economists, was also followed by an easing of interest rates and a fall in sterling.

The one similarity with 1981 is the combination of high interest rates and pressures towards recession. But the differences are very much greater. In 1981 the Budget was still in heavy structural deficit and a strong policy pointer towards long-run balance was required. Now however the Budget is showing a surplus and any required long-run correction could be in the opposite direction.

A more important difference is that, just before the 1981 Budget, sterling had overshot upwards. Once British industry had received its salutary shock, the main need was to bring the pound down to levels with which business could locate danger prevail. The biggest threat to economic policy comes from the alarmingly downward drift of sterling, and it is this that ought to be the focus of attention rather than the balance of payments.

Sterling has been on a worrying course since the last rise in base rates to 15 per cent on October 5, in the wake of a Bundesbank increase, failed to steady the currency. It was, in fact, reasonably stable immediately afterwards, but was fatally undermined by unintended weekend reports that the Prime Minister and Sir Alan Walters were opposed to any further action to prevent the pound falling.

The following week, that of the Conservative Party conference, when I was mercifully in America, sterling went below Nigel Lawson's preferred DM 3 level. After he resigned his enemies were delighted to report that sterling had stabilised in a slightly lower range. Alas for the British economy, their triumph was short-lived, as sterling has since been approaching the DM 2.90 level. For a year ahead it is quoted at well below DM 2.70.

Even these rates would be tolerable, though undesirable, if there was some intention to stabilise the pound there, perhaps in conjunction with full EMS membership in the second half of 1990. It would mean that inflation would take longer to converge on European levels, but it would mean that there would be gyrations, but converge it eventually would.

The really frightening prospect is of sterling continuing to sag with no end in sight as high expected depreciation, high interest rates and high inflation combine together in a self-reinforcing cycle.

Nor has the decline been only against the D-Mark. Despite the dollar's recent weakness, sterling has also been weak against the Bank of England Index and is now near the low point reached in the winter of 1989 (after the rebound from the oil price drop and before the run up to the last election). Virtually all the ground gained since has been subsequently lost.

The political uncertainties about

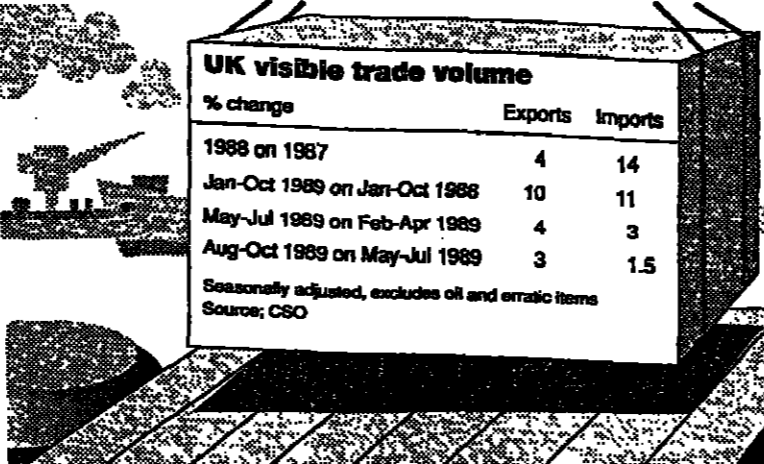
the Prime Minister's position and the next election are said to be an adverse factor. But the pound is hardly helped when Mrs Thatcher in her interview with *The Times* last Friday once more dismisses any idea of interest rate policy being influenced by a concern for the exchange rate. Nor is it helped when she offers fulsome and unqualified praise for Sir Alan Walters, despite the latter's scarcely concealed advocacy of lower sterling and lower interest rates. She obviously did prefer Sir Alan to her own Chancellor.

But it can hardly be a good thing that sterling should have fallen further after a recorded trade deficit lower than market analysts had expected. Some self-proclaimed Government sympathisers see the clue to election victory in a tough fiscal policy in 1990 followed by 18 months of falling interest rates, even at the expense of sinking sterling. This could work in the very crude sense that falling mortgage rates distort headline inflation rates downwards (just as rising rates distort them upwards). The inflationary effects of falling sterling are more fundamental, but may be delayed until after an election.

What this pretty little theory leaves out is the possibility of a sterling downturn getting out of hand. Politically, the Government cannot be sure of rooting enough of the people enough of the time to win by such cosmetics. As a gentle reminder, the basic inflation rate, excluding mortgage interest - now 6.1 per cent - will feature regularly in this column, together with an estimate of the underlying rate.

Meanwhile, the October trade figures did not add much to one's knowledge of the British economy. But just as the Government cannot be sure of rooting enough of the people enough of the time to win by such cosmetics, as a gentle reminder, the basic inflation rate, excluding mortgage interest - now 6.1 per cent - will feature regularly in this column, together with an estimate of the underlying rate.

The differences with 1981, when a tough Budget helped interest rates fall, are greater than the similarities



As % of GDP	Average				Change	
	1965-75	1979	1986	1989	79-89	86-89
Personal consumption	59.1	59.0	62.3	65.3	+6.3	+3.0
Government consumption	21.6	21.2	20.5	18.8	-2.4	-1.7
Fixed investment	18.4	17.1	16.7	19.9	+2.8	+3.2
Stockbuilding	0.7	1.0	0.2	0.8	-0.2	+0.6
Balance of trade in goods and services	0.3	1.5	0.3	-4.7	-6.2	-5.0
Domestic savings	19.3	19.8	17.2	15.9	-3.9	-1.3

Source: London Business School

ance of payments, I do not of course mean the true figures or even a best guess, but the estimates published by the Statistical Office with a £15bn unallocated balancing item.

All one can say beyond that is that the current deficit is somewhere between level pegging and on a slightly improving trend. The best indicator (in the top table) is the one which shows volume changes, excluding oil and other erratic items. In the first 10 months of the year, imports rose very slightly more than exports. But in the shorter period since the Easter quarter, the quarterly growth of exports has been somewhat higher.

Professor Wynne Godley has objected to my saying on the basis of the figures in the Autumn Statement that the current deficit reflects rising investment, partly financed from overseas, rather than falling savings.

(Letters to the Editor, November 21.) Readers are entitled to ask why there are such large differences on apparently factual matters.

One reason is simply that of periods compared. My comparison was with 1986, the last year of recorded current account balance, while Professor Godley's was with 1979 and earlier years. The latter comparison is appropriate if one is appraising the Thatcher Government's record (as I have attempted to do in my chapter in *The Thatcher Effect*, edited by Kavanagh and Seldon, published this year by OUP). The former is more relevant if one is examining the swing in the deficit.

Another difference is that I looked at so-called nominal magnitudes (that is actual cash) while Godley looked at constant price estimates. Although I do have a preference for nominal magnitudes, especially when discuss-

ing financial policy, the main reason for my procedure is that official estimates for savings are published in nominal terms. Estimates of consumption, which is the difference between income and savings (and which Godley prefers to use) are usually published in constant prices. A third difference, less important in practice, is that I have used estimates for 1989 rather than forecasts for 1990.

But to meet Godley more than half way, I am including a table at constant 1985 prices, specially prepared by the London Business School. I should add that in this sort of table the balance of payments deficit is overstated because it does not include overseas interest, profits, and dividends which have fluctuated between 1% and 1 1/2% per cent of GDP.

The table does show that, of the 5 percentage points deterioration in the current balances between 1986 and 1989, some 1.3 points are due to a fall in domestic savings, but more than 3.7 points are due to increased investment and stock-building (rounding downwards for consistency). If one looks at nominal magnitudes instead, there is little change in the savings ratio and a smaller trade deterioration. But on either basis savings are much higher than most commentators, who forget about the corporate and public sector contributions, and only look at personal savings, assume.

Another reason, however, why the fall in the savings ratio is so modest is that the rise in personal consumption has been paid for by a rise in government consumption. Whatever the political pros and cons, the picture remains one of an investment boom financed by overseas borrowing.

If that is all that has happened, where does the inflationary threat come from? It cannot be seen from a table of percentages. It arises basically from a growth in demand and output too great for the economy's capacity, which has taken the level of labour and capacity utilisation above the so-called natural rates consistent with non-accelerating inflation.

The important question is whether the level of interest rates required to finance the current deficit is excessive for inflation control purposes. Up to now it has not been. But how do we escape from a circle of high expected inflation, large expected sterling depreciation, and high nominal interest rates? To secure a more virtuous circle of lower inflation, smaller expected depreciation, and lower nominal interest rates, would require some shock to the system. In the absence of Japanese style flexibility in the labour market, the possible shocks are a severe 1980-81 type recession or some official indication of a floor to sterling, to which the Prime Minister seems resolutely opposed.

But even if she were induced by an unexpected display of Cabinet virility to change her mind, interest rates would remain intermittently high until credibility was restored. The more likely prospect at present is little beneficial shock of any kind, a modest recession, if one occurs at all, and a continuing inflation differential above competitor countries.

LOMBARD

# An explosive recipe

By Michael Prowse

MR KENNETH CLARKE, Britain's Health Secretary, last week hailed the National Health Service Bill as one of the most important milestones in the development of the NHS. It is perhaps better regarded as a messy compromise which will alienate potential supporters of the Government without resolving fundamental health care dilemmas.

The legislation is supposedly a response to the 1987-88 funding crisis, which led to a politically embarrassing spate of ward closures. Mrs Thatcher managed to defuse the crisis only by promising a far-reaching review of the financing of the NHS. Yet neither February's white paper nor last week's bill addresses this crucial issue. Mr Clarke's line is that financial worries are over because he won a respectable increase in this year's public expenditure changes.

This really will not do. Rising aspirations, improvements in medical technology, and the ageing of the population are likely to cause steep increases in the demand for health care. Yet the Government remains committed to reducing the burden of taxation as a share of gross domestic product. This circle will prove desperately hard to square in anything but the short term.

There are two possible solutions. Right-wingers argue that the supply/demand imbalance can be corrected only if the public sector stops rationing health care. On this view, individuals must accept responsibility for deciding how much they wish to spend on health. The NHS should thus be privatised and replaced by a regulated private health insurance market. Subsidies would ensure that everybody could afford a basic level of care; those with means who wanted something better would have to pay for it. The crucial point is that there would be no overall cap on spending.

Critics on the left regard private insurance as inhumane and inefficient. But they are not uniformly content with existing budgetary arrangements. The solution increasingly favoured in Labour Party circles is some form of earmarking of NHS revenue. It

would be possible, for example, to finance health care either through national insurance contributions or a specific income-related health levy. The advantage would be that revenue, instead of barely keeping pace with price rises, would then automatically increase in line with earnings. Paradoxically, Mr Clarke's bill, while seeking value for money, is likely to accentuate behavioural constraints and increase pressure for radical changes in the financing of the NHS. The development of an internal market will necessitate heavy expenditure on new staff, information technology and billing systems. Most countries with competitive delivery systems spend a much higher proportion of GDP on health care than the UK and this is partially a reflection of higher administrative costs.

Behavioural changes will be most important. In the past, health authorities and hospitals have been allocated budgets and expected to maximise health care subject to their cash constraints. The absence of significant competition has helped hold costs down. Salaries have been abnormally low by international standards precisely because hospitals have not had to bid against each other for highly qualified medical staff. The health service has also been able to economise on non-medical items: compare NHS dowdiness with the opulence of US hospitals.

In a competitive regime the culture will be very different. Marketing and advertising will become crucial tools for generating business. Since income will depend on turnover, you can be sure the amount of treatment provided will rise steeply. The phenomenon of "supplier-induced demand" is a well documented fact of market regimes and is unlikely to be effectively countered by health authorities' new role as purchasing agents. Some of the strain may be lifted by an expansion of the small private health care market. But this does not alter the fact that Mr Clarke is greatly stimulating the demand for health care without relaxing its financing constraints. This is likely to prove an explosive recipe.

## LETTERS

### Chambers' status

From Mr Eric Dodson.  
Sir, Mr Anthony Platt argues fully and convincingly for public law status for British chambers of commerce (November 7). I and others, during our periods of service in the chamber movement, have long advocated this as a means of giving visiting European chambers of commerce the same as that related by Mr Platt. Indeed, I found it uncomfortable to try to explain to their officers the reason for our apparent feebleness in coming usually with the impression that the UK Government resisted all attempts to achieve public law status by an expressed reluctance, as a matter of principle, to intro-

duce any degree of compulsion. Perhaps a portion of the arguments will eventually produce some result by the time of the assumed completion of the internal market. But, before then, consideration should again be given to extending the activities of British chambers, initially even on a voluntary basis - for example, by registering particulars of partnership and individual businesses; a most useful procedure for the protection of the public which was lost with the ill-judged abolition of the Business Names Act. Eric H. Dodson, *The Knoll, Ladythorn Crescent, Bramhall, Cheshire*

### London loses out

From Mr Stephen Moss.  
Sir, Mr Tony Travers draws attention (Letters, November 23) to one aspect of how London loses out - the low Uniform Business Rate (UBR). Other important aspects deserve attention. UBR revenues go into central Government coffers for redistribution on a basis wholly unconnected with the size of the business rate base. This removes local authority direct control over expenditure of business rates - and motivation to talk to the business community. Annual rate rises, capped

ungenerously at 20 per cent plus inflation, will encourage yet more companies in London to relocate. Businesses wishing to continue my regular (and artificial) disincentive to growth and mobility imposed upon them by a provision restricting the 20 per cent a year ceiling only to those in occupation at April 1 1990. Businesses moving after that date will instantly pay the full rate of UBR. What has London done to deserve this treatment? Stephen Moss, *Kensington & Chelsea Chamber of Trade & Commerce, Cromwell Place, SW7*

### Confidence-building by mail

From Mr S.G. Hannon.  
Sir, The Royal Mail has re-introduced Sunday collections because its customers told us they wanted it (Letters, November 15). The service is a direct response to strong customer demand shown in national surveys, and backed by the Post Office Users' National Council as well as the Union of Communication Workers in a ballot of members. On Sunday November 19 the first day of operation in five districts, volunteer postal staff collected some 155,000 letters - which goes to prove that demand. But this important investment in improving service is just one of a whole range of measures we are already introducing to boost letter reliability for all our customers, including businesses, throughout the week, for which the Royal Mail is spending £65m in

the next 12 months alone: Making more first collections by van instead of using postmen on foot, and improving collection arrangements; Improving deliveries in areas where we have difficulties in recruiting and retaining staff; Improving delivery service on Saturdays; Postal Planners, showing best posting times to connect with transport links, which are being delivered to all 24m addresses in the UK; Faster direct road links for high volume mail between important districts. We are confident that these combined measures will continue to build customer confidence in the Royal Mail's ability to give a "decent, uninterrupted service." S.G. Hannon, *Royal Mail Letters, 39 Grosvenor Place, SW1*

### 'A vague law, applied vaguely'

From Mr Fergus Randolph.  
Sir, Peter Montagnon, on rules of origin (November 23) gives a good description of a difficult, important area of law in international trade. But some confusion appears to have arisen over the Kyoto convention issue. The EC's rules on origin are encapsulated in council regulation 802/68. These rules came into force on July 1 1968, some six and a half years before the Kyoto convention and some nine years before the specific rules on origin, contained in an annex to the Convention, were accepted by the EC. The council regulation has not been amended by the terms in the convention, and thus it cannot be said that "The EC uses the internationally agreed Kyoto convention when deciding on its origin rules." (It is understandable that your correspondent was under such an impression, given the rather woolly attitude of the European Commission on this subject.) The relationship between council regulation 802/68 and the Kyoto convention has never been made clear.

Although the basic definitions of origin are similar, the criteria used for each determination differ markedly. The European Court of Justice has declared, for example, that one of the criteria used in the Kyoto convention as being determinant of origin cannot be so used under council regulation 802/68. In a recent case before the European Court it was argued that the EC is bound by the Kyoto convention, and must thus change its rules on origin. Judgment has not yet been given. It is lamentable that the EC, one of the largest trading blocs in the world, has been unable to resolve this question. As Peter Montagnon correctly says, the present situation gives rise to cries of "Protectionism" from third countries; difficult to silence. I hope the proposal put to the Commission on changes to the rules on origin will bear some fruit, and that the ultimate non-tariff barrier of a vague law, applied vaguely, will change. Fergus Randolph, *Avenue de la Joyeuse Entrée 8, B-1040 Brussels, Belgium*

### Public purchasing in the EC

From Mr Tasos Bisopoulos.  
Sir, Guy de Jonquière's report on public procurement in the EC (November 13) is a comprehensive account of this sector in the European economy, but gives only the view from Brussels, and scant consideration to developments and prospects in each EC country. The differences in public purchasing among member states is a reality overlooked by the "lawyer's approach" adopted by the Commission. This approach has proved unworkable for 20 years. Existing differences in structure and attitudes in each country have persuaded public officials and contractors that any honest attempt to open up this market would not be followed by other countries. Furthermore, in the UK there are only 700 large procurement entities which deal with bulk purchases and value for money; in Germany and Italy there are more than 20,000 similar purchasing entities which, being smaller, are free to "buy local," restricting opportunities for firms from other member states. Mrs Thatcher rightly stressed this reality in the recent "Walden interview."

Instead of the Brussels uniform approach, a localised strategy would be more efficient. Commercial incentives for contractors to bid in other states, decentralised bodies which would monitor this area with rewards for those who comply (and punishments for infringements), would build on Commission policy of promoting more information to contractors. Do we really mean to bring about a prosperous united Europe if we cannot even agree on such simple steps? Tasos Bisopoulos, *38 Doughty Street, WC1*

### Healthy wealth

From Mr R.J. Shanks.  
Sir, Mr J. Rowden (Letters, November 23) may be right to say that "only healthy economic growth can provide the wealth needed to promote environmental improvement." The word "healthy" is important. So much economic growth and "progress" is unhealthy in environmental terms. R.J. Shanks, *6 Rodney Gardens, Eastcote, Pinner, Middlesex*

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Janet Bush on Wall Street

## A lesson for stock analysts

PERHAPS the oddest stock last week was Texas Instruments. On Tuesday, it first slumped on news that the company would take a \$55m pre-tax charge in the fourth quarter and that it was planning to cut its workforce by about 1,500 people. Then, mysteriously, the stock jumped to close 3 1/4% higher at \$51.

The fireworks really started on Wednesday when Texas Instruments jumped 5 1/2% to \$53 3/4. By then it had been reported in US morning editions that the company had issued with a Japanese patent which it believed covers "virtually all integrated" circuits made or used in Japan.

Although Texas Instruments was very low key about the whole thing, the community of the investment community is a tale in itself. It took an exceedingly long time for Wall Street's army of stock analysts to find out about this dramatic development.

The news first hit the world's financial press overnight on Tuesday, when it appeared on the front page of the Japanese newspaper Nihon Keizai Shimbun. Notwithstanding the fact that most major Wall Street investment banks have offices in Tokyo and presumably read the local business press, the news did not filter into the company's share price until the afternoon session on the New York Stock Exchange - and then only when representatives of Nomura Securities in Tokyo called US analysts to ask them for a judgement about what the potential impact could be.

What is even more surprising was that the patent was actually issued on October 30, fully three weeks before anybody on Wall Street knew about it.

When asked about the story by the Wall Street Journal, Texas Instruments rather sweetly said that they had not announced it because they did not want to "blow their own horn".

In these days of lightning communication and instantaneous transmission of knowledge from Tokyo to Lower Manhattan, it is rather strange that the army of stock analysts at brokerage houses were so slow on the uptake. One by one, analysts were being known to get it wrong on so many occasions that a little slip-up like the one over Texas Instruments should not be particularly surprising.

One of the most celebrated examples of analysts failing to do their job properly was the case of Atlantic Richfield. In 1965, its stock was trading at around \$10 a share. Only a year later, it had plunged to \$8. The reason for this is that nobody on Wall Street had figured out a crucial error in the design and planning of Atlantic Richfield's Alaska pipeline: the company had not taken into account the migration path of the caribou, which eventually led to a complete redesign of the pipeline.

Mr Tony Hirschler, now head of Brandywine Asset Management, a small Wilmington, Delaware money management concern devoted to investing in stocks with low price/earnings ratios, used the Atlantic Richfield case in an essay in 1980 highlighting one perennial shortcoming in the community of stock analysts.

The "caribou" eventually visit most stocks, and when they visit one with a very high P/E multiple, the consequences can be drastic. Yet most analysts continue to extrapolate past earnings increases into the future," he wrote.

There is a famous anecdote told on Wall Street about Mr Norton Simon, the wealthy industrialist, who, it is said, sat in his Jensen outside Grauman's Chinese Theatre - one of the most famous movie houses in the world and now called Mann's since it was taken over - on Hollywood Boulevard.

## Gandhi's Congress faces defeat

By David Housego in New Delhi

INDIA'S Congress Party, led by Prime Minister Rajiv Gandhi, appeared to be heading for defeat last night in a general election that seems likely to herald a period of political instability in the country.

The possibility of defeat cast doubts on the future of Mr Gandhi as party leader and on the Gandhi dynasty which has held power since India's independence from Britain in 1947 with one brief, 29-month interruption in 1977-80. Early trends in the counting of votes suggested that the Congress Party would win about 200 of the 525 seats being contested, compared with the 415 it achieved in a landslide victory in 1984.

Though the Congress would remain the single largest party in the National Assembly, the main opposition parties would hold sufficient seats to block its attempts to form a government.

In Mr Gandhi's own constituency of Amethi in the north, re-polling is to take place today in 97 districts - 10 per cent of the constituency - after the opposition alleged "massive rigging". The local district magistrate and the superintendent of police have both been dismissed.

Opposition representatives claimed last night that the National Front, the group of opposition parties under Mr V.P. Singh, would be in a position to form a government. The Front is likely to emerge as the second largest group in the National Assembly but would need the support of both the Hindu militant BJP party and the Marxists to form a government.

Most observers believe opposition consultations over the

coming week would focus on the National Front forming a minority administration with support from the BJP on the right and the Marxists on the left. This has long been seen as the most unstable arrangement that could emerge from the election.

The Congress Party strengthened its position in the south but had major reverses in the north and setbacks in the east and west.

The defeat of opposition-backed state governments in the south and of the Congress at the national level led commentators to describe the election "as a vote for change". In the north Congress was doing badly in the Hindi speaking states of Rajasthan, Madhya Pradesh, Bihar and to a lesser extent Uttar Pradesh.

A surprise was the success of the BJP which is likely to

increase its strength in the new Parliament from 2 to over 70. The BJP has been campaigning on a platform of Hindu fundamentalism.

Overall, the swing against the Congress was between 8 and 10 per cent. In the north, the minority Moslem population seems to have shifted against the government as a result of recent Hindu-Muslim clashes over plans to build a Hindu shrine at Ayodhya on the site of a mosque.

The election, staggered over three days since last Wednesday, was accompanied by unprecedented violence in which more than 100 people were killed and by widespread electoral fraud. The Chief Election Commissioner ordered re-polling in 1,124 districts after the first two days of voting.

Background, Page 2; Editorial comment, Page 18

## UK seeks £2bn finance to save armaments deal with Saudis

By Andrew Gowers in Riyadh and Victor Mallet in London

THE British Government is making urgent efforts to arrange a bank loan of around £2bn (\$3,150m) to finance continued Saudi Arabian purchases of military equipment under the UK's huge Al-Yamamah defence contract.

The loan, which would be backed by British banks and the UK's Export Credits Guarantee Department, would make up for sizeable Saudi payment shortfalls caused by weak oil prices.

It is not yet clear whether the borrower would be the Kingdom itself or the contractors involved in the project. But observers in Riyadh say a new financing package is now essential for the continuation of its present form of the Al-Yamamah deal, under which Britain agreed to supply Saudi Arabia with 120 Tornado fighter aircraft and a range of other equipment, including jet trainers, minihunters, helicopters and base facilities.

Without such a package or a sharp rise in oil prices, it is likely that deliveries of hardware to Saudi Arabia will be slowed down, and it is even possible that parts of the contract might be cancelled.

The way the issue is resolved will thus be of critical importance for British Aerospace, as

lead contractor for Al-Yamamah, and for a number of other UK companies involved in the deal, including Westland and Vespene-Thomson.

The first Al-Yamamah agreement was initiated in 1985, but it was extended under a new contract last year to become Britain's biggest ever arms deal, with a possible final value well in excess of £15bn.

Difficulties centre on the barter arrangement under which Saudi Arabia is paying for Al-Yamamah with 400,000 barrels a day of oil. The fall in world oil prices in 1985-86 has resulted in a significant mismatch between the value of British deliveries and the flow of cash from the Saudi crude, and an increasing deficit on the project at BAE.

Talks on the problem between the two governments and the companies involved have been going on for many months in a confidential and secret. But the British Government is now understood to be anxious to put new financing arrangements - entailing either a loan or a significant increase in oil liftings - in place by the end of the year.

Mr Alan Thomas, head of defence export sales at Britain's Ministry of Defence, is believed to have pressed the

## Defence has 'only small role' in US budget cuts

By Peter Riddell, US Editor, in Washington

THE "peace dividend", the savings in US defence expenditure as a result of the lowering in East/West tensions, will make only a small contribution to reducing the US budget deficit in the immediate future, Mr Richard Darman, the Budget Director, has suggested.

Speaking at the Bush Administration prepares its budget for submission on January 8, Mr Darman warned against expecting early large savings cuts next October. This has big implications for the prospects of cutting the deficit, which is generally regarded as one of the US's economic priorities.

Mr Darman said that in the near term (referring to the 1991 fiscal year starting next October) defence savings were going to be "small, of the order of \$10bn, not the kinds of large numbers that people are assuming".

This compares with the \$50bn savings cuts next October Darman has estimated will be needed to get down to near the target of a \$64bn federal deficit for fiscal 1991, as laid down in the Gramm-Rudman law.

Mr Darman sought to distinguish between the size of short-term cuts on defence expenditure with the possibility of "substantial savings over five years, though nowhere near as large as people are assuming".

Mr Darman said the Pentagon budget is "very, very slow to change in either direction. If it's going up, it doesn't go up as quickly as people think. If it's coming down, it doesn't come down as quickly as people think".

He discounted recent reports of \$150bn and \$180bn savings in the early-to-mid 1990s, which, he said, were in relation to Defence Department plans and not in relation to the likely available resources. The implication is that some of the projected cuts might be from planned totals which were anyway unrealistic.

Mr Darman's estimates of defence savings also indicate a tight squeeze on domestic programmes since there is no sign of President George Bush moving from his "no new taxes" pledge. The Budget director claimed that "the odds are higher than 95 per cent that we'll be able to present a budget without new taxes".

There may still be minor revenue adjustments of the type which accounted for two-fifths of the \$14.7bn deficit reduction for fiscal 1990 approved by Congress last week.

In an effort to hold down spending, Mr Darman last week proposed setting aside "a limited pool" of money for high priority programmes. Heads of departments and agencies would appear before President Bush to argue their case for a share of this pool.

## Czech spirit blooms

Continued from Page 1

night of November 17. Nobody is frightened any more. Nothing is taboo. The taboos are disappearing.

Even the police are speaking out.

During yet another massive meeting on Letenske Plain, a young policeman yesterday spoke in a candid and open manner to the crowd.

"I was taught to fight criminals, not to beat up peaceful demonstrators," he told the snow-covered tens of thousands.

"We cannot judge what we are doing. It is Them Up There who are giving the orders."

"Who are they? Who are they?" the crowd spontaneously questioned back.

"I don't know. I don't know," the young man replied, completely lost for an answer.

But the crowds knew what they wanted. "Enough of Them! Enough of Them!" And as if they still have to shake off the pent-up anger which has accumulated over the years, many of them proceeded to form a long human chain across to Hradcany.

But they still wanted more. And they will have it today, when the Czech and Slovak nations will stage a general strike.

Mr Adamec, who in a brave gesture, stood on the podium yesterday with Mr Havel and Mr Dubcek, nearly spilt his

entree into public view.

"I am glad that Monday's strike will be a peaceful demonstration and not a confrontation. But there is no need for a two-hour strike. Just a couple of minutes."

The crowd were going to have none of this. Father Janak said that a long-sustained opposition force who has now been catapulted into the limelight, chastised the Prime Minister.

"We will not use the methods of the Communists to tell people what to do. Let the strike committees decide," he said. The crowds loved these words, words which would have been mutterable even a week ago.

## Britain and Vietnam agree cash deal

Continued from Page 1

such people could be considered humanitarian.

Hong Kong, there is growing unrest among the boat people in the camps. This, and protests against compulsory repatriation, could make it more difficult for the colony's security forces to start repatriation without a violent reaction.

More than 2,000 boat people started to refuse government food supplies at the weekend, although their action falls short of a full hunger strike because they have access to privately supplied food. In a separate development, there was a pitched battle in a tented camp between rival groups

from Vietnam's Haiphong and Quang Ninh provinces.

Hong Kong wants to act within two or three weeks so that enough Vietnamese arrive back in their home towns and villages by next spring to deter more boat people from setting out when the weather and tides improve.

Officials fear that at least 30,000 more will arrive by next summer unless they are put off by the start of a compulsory repatriation programme. Hong Kong's local legislators have said they are not prepared to approve the fresh funds needed for them to be looked after.

Around 35,000 have arrived in the past year, including an

unseasonably high total of 335 this month. There are now 44,000 boat people in camps who are being screened to determine if they are genuine refugees qualifying for resettlement or are economic migrants who, under a Hong Kong policy introduced 17 months ago, should be sent home.

Judging from the results of 6,000 people screened so far, only about 10 per cent will qualify as refugees, which means that about 40,000 are due to go home. So far only 500 have been voluntarily repatriated.

Hong Kong has agreed terms for the compulsory repatriation with Vietnam.

## World Weather

Location	Temp	Wind	Cloud	Temp	Wind	Cloud
Alaska	10	7	7	40	10	7
Algeria	24	7	7	40	10	7
Amsterdam	10	7	7	40	10	7
Atlanta	10	7	7	40	10	7
Bahia	25	7	7	40	10	7
Bangkok	28	7	7	40	10	7
Buenos Aires	10	7	7	40	10	7
Calcutta	28	7	7	40	10	7
Caracas	28	7	7	40	10	7
Chicago	10	7	7	40	10	7
Copenhagen	10	7	7	40	10	7
Hong Kong	28	7	7	40	10	7
London	10	7	7	40	10	7
Los Angeles	10	7	7	40	10	7
Madras	28	7	7	40	10	7
Manila	28	7	7	40	10	7
Mumbai	28	7	7	40	10	7
Osaka	10	7	7	40	10	7
Paris	10	7	7	40	10	7
Perth	10	7	7	40	10	7
Rangoon	28	7	7	40	10	7
Singapore	28	7	7	40	10	7
Tokyo	10	7	7	40	10	7
Washington	10	7	7	40	10	7
Yokohama	10	7	7	40	10	7

## Finance chief set to quit

Continued from Page 1

new mandate next March when his current term runs out.

Mr Pierson, who has been one of the principal architects of the recent commercial successes of the aircraft group, appears so far not to have made up his mind whether to seek a new term or not.

Should he decide to leave, the consortium is likely to face further upheaval in the form of a new power struggle between the four partners.

The four partners decided to give the go-ahead for the new A-321 at an extended meeting

in Frankfurt which ended last Saturday. The consortium was widely expected to launch the new programme before the end of this month.

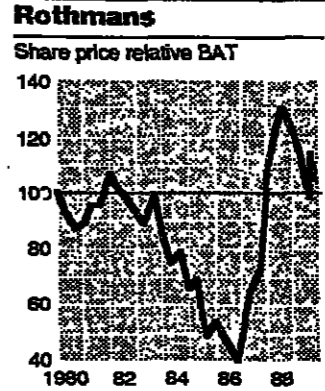
Airbus has already secured 107 firm orders for the A-321, which costs about \$45m per aircraft, and additional commitments for 74 more aircraft.

The group originally said it needed at least 40 firm orders to launch the new programme.

Airbus said yesterday it was now finalising with various banks the details of the funding for the A-321 programme.

## THE LEX COLUMN

### Deciphering gold's mixed signals



Share price relative to BAT

1980 82 84 86 88

The financial markets are rightly puzzled by the confusing signals coming out of the gold market. At a time when base metal prices are writing recessionary fears and peace is breaking out all over the place, the gold price has suddenly woken up from a two year old slumber and risen by over \$50 per ounce in little more than a month. The FT Gold Mines index, which often seems to be in near terminal decline, has jumped by 45 per cent over the same period.

Predicting where the gold price goes next is a mug's game. But that does not mean that the yellow metal's price fluctuations should be totally ignored. The jump in the price may well be just an aberration, but it could just mean that some investors want more gold, like some people want a bit more disaster insurance.

Gold thrives on uncertainty, and while the long-term impact of any cutback in defence spending around the world is positive, there is more than an average amount of political and financial uncertainty around, currently.

For a start, the 15 per cent jump in the gold price since last month's one-day drop of 7 per cent on Wall Street, contrasts with the minimal rise in the gold price after the Dow's 23 per cent one-day fall in 1987. The recent rise in gold could be another signal that the equity markets are not in as robust a condition as two years ago. Certainly, the US corporate sector is more highly leveraged than for a very long time, and one of its main sources of refinancing - the junk bond market - has almost dried up.

The jump in the gold price also does not fit easily with the conventional wisdom that global inflation will decline next year. Perhaps, gold is reacting to the fact that real interest rates are considerably lower than a year ago. Soviet inflation is accelerating, or a perception that the Federal Reserve is now becoming more worried about recession than inflation.

However, gold is probably a better barometer of exchange rates than anything else, and the strongest signal that it may be transmitting is that the dollar's period of surprising strength is over.

It is also true that the shock of change, even if temporary, can be a healthy stimulus. But we have heard enough of the buyout as an exercise in courageous self-termination. It is just a way to make a killing, quicker than most.

### Rothmans Int'l

When Swiss-based Rothmans' offer for Rothmans closes in less than a fortnight, almost certainly leaving Rothmans with 69 per cent control, the real battle will have only just begun. Rothmans' tantalising offer document promised

to Hoare Govett, Rothmans could be worth £2.35 a share, a long way from Friday's closing price of £6.52. In theory, Richmond should be eager to close the valuation gap, by selling or floating the luxury goods interests. The problem for the holders of the 31 per cent of Rothmans likely to be left in outside hands, is that their notions of shareholder value could fall to coincide with Richmond's.

### Buyouts

Last week's proposed takeover of UK Paper by Metis-Serla of Finland revives lurking doubts about the whole principle of the management buyout. When it was bought out from Bowater, UK Paper was hailed as a heroic step in the revival of the independent UK paper industry. It has now decided that it is too small for independent life after all, and is heading back into the embrace of a big corporation.

There are numerous parallels: Caradon, bought out from Reed and sold to MFG Group; Premier, bought out from Cadbury and sold to Hillsdown. Both UK Paper and Caradon had previously gone public again within the conventional two or three year period, thus realising very large sums on paper for the managers. These sums - plus the normal premium for takeover - were then converted to hard cash by selling out.

If buyouts are such a virtuous process of rejuvenation, it is not clear why managers should call a halt in this way rather than leave their money in and continue to multiply it. Indeed, it is not quite clear why they should go public in the first place. Granted, institutional backers generally want the option of taking part in their five years at most. But Unipart, for instance - bought out from Rover in 1987 - has just quietly arranged a re-levelling exercise - thus satisfying its original backers and leaving control with the management.

The cynical view of the standard three-year buyout - a burst of unwarranted effort followed by a relapse into corporatism - need not be the whole story. Both UK Paper and Caradon will end up with more appropriate parents than before, even if the method of changing ownership seems rather clumsy. It is also true that the shock of change, even if temporary, can be a healthy stimulus. But we have heard enough of the buyout as an exercise in courageous self-termination. It is just a way to make a killing, quicker than most.



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# FINANCIAL TIMES COMPANIES & MARKETS

Monday November 27 1989



## INSIDE Man who must control the flow

The primary duty of Mr Ian Byatt (left), Director General of Water Services, is to make sure that the soon-to-be-privatised water and sewerage businesses of England and Wales can carry out and fund operations. His principal weapon is the cap on water company price increases, which he will both set and review. It sounds simple - and advocates of investment in water believe the Water Act ensures solid returns for shareholders. Yet, in spite of these apparent guarantees, Mr Byatt has already found himself at the centre of political and financial debates. Page 25

**Japanese banks feels the pinch**  
Japanese banks' profits have been squeezed by rising interest rates, forcing some of them to announce their first reductions in interim net profits since 1981, the year they started reporting half-year figures. The increases in interest rates pushed up the cost of money at a time when the proportion of funds raised at market rates, as opposed to artificially low regulated rates, is rising rapidly due to liberalisation. Stefan Wagstyl reports. Page 25

**Private seats on the gravy train**



Rumours of losses and imminent job-cuts abound in the Euro market. Everyone agrees there are just too many banks chasing too little business. But, explains Andrew Freeman, many of the larger Eurobond houses have quietly honed ways of improving their overall profits performance. More than a handful of houses admitted last week that in 1989 they have done rather more private placement than public business. They say they are making good profits in this area, so there is much less reason to believe that they are planning large cuts elsewhere. Why shut down a syndicate department in public, when you can discreetly disguise the possession of a first class seat on a gravy train? Page 22

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## Dark side of the enchanted forest

James Buchan examines the problems facing International Paper

Spare a thought for International Paper. The laughing-stock of the world paper industry for a generation, the company has recently been looking good. For 10 years, it poured astonishing amounts of capital into a run-down network of pulp, paper and board plants. And it is reaping the benefit. With booming markets last year, International Paper's sales increased by 23 per cent to \$5.5bn, and its profits almost doubled to \$754m.

But just when the company's luck really seems to be mending, there are ominous signs in the market. US economic activity is slowing down and paper customers are forecasting price competition in the prospect of new capacity: several new or reconditioned paper-making machines start up next year and in 1991. Already prices are stagnant or falling in the company's main commodity markets, such as linerboard (used for boxes) and uncoated white papers for printing and writing.

Georgia-Pacific's \$3.5bn takeover offer for Great Northern Nekeose, though it has yet to be accepted, could create an aggressive new competitor with \$15bn in sales and the power to disrupt these commodity markets where International Paper has big but not commanding shares.

Above all, the company has no friends at all on Wall Street.

International Paper could have burned the \$10.7bn it has spent on its 28 mills and on acquisitions in the 1980s for all the value it has created in the stock market. At just under \$60 a share, International Paper is worth \$5.4bn on Wall Street: billions of dollars of capital spending have gone up in smoke.

For Mr John Georges, the chairman of International Paper, Wall Street's attitude is disheartening. In an interview last week at International Paper's headquarters in the New York suburbs, Mr Georges, who is 68, said the stock market may be too bearish about world paper markets and is causing him to think the point with International Paper.

An unprecedented capital programme, a big push into Western Europe and a persistent move to more specialised products, have made the company much better equipped to withstand a downturn, he says. International Paper is not the boom-and-bust cyclical company it was.

"People remember the severe recession of the early 1980s," he says. "They're using that as a benchmark for us and my gut feeling is that it's not going to be so bad."

International Paper, which is the world's largest paper company and the biggest corporate

landowner, began life at the end of the 19th century as a conglomerate of New York and New England paper mills. For two generations, it bought timberland, cut trees and built mills: it was evidently managed without distinction but without great mishap. Towards the end of the 1960s, however, the company attempted to diversify and did run into problems.

It brought in a retired chairman of AT & T, who was succeeded in turn by professionals from Mobil, GE and DuPont. International Paper became a laboratory for managerial experiments cooked up in these large-houses of management talent. There was more diversification. The mills, mostly built in the 1920s and 1930s, were neglected. By the end of the 1970s, the company probably had the highest operating costs in the industry. It was slow, weak and defensive.

It was Mr Edwin Gee, who became president in 1978, and Mr Georges, who arrived the next year and took the company back to paper. DuPonters both, they related more than \$2bn by selling off businesses, oil and gas reserves, medical products, financial services and, in 1981, the big and volatile Canadian newsprint operation. With the money, and with internally generated profits, they bought a good linerboard mill and acres of southern pine

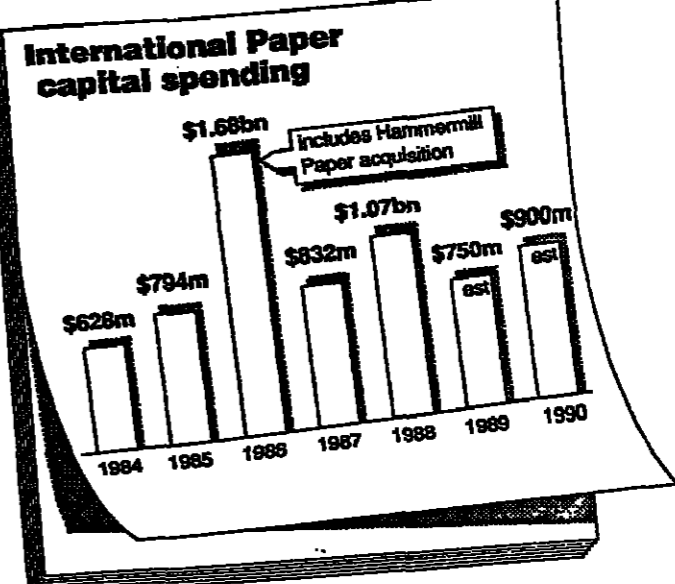
forest. In addition they rebuilt the collapsing paper-and-pulp-making machines.

Their timing could not have been worse. Interest rates were soaring, and a \$600m linerboard mill in Mansfield, Louisiana opened in 1981 punctually in time for recession. A bungled \$500m conversion of an old mill in Georgetown, South Carolina, cost the company huge losses.

But the investment programme, which Mr Georges continued when he took over as chief executive in 1984, has worked wonders for International Paper's cost base. And in a commodity business such as most of the paper industry, low production costs are far more important than size.

While fighting to be low-cost producer in the commodity grades, Mr Georges is also trying to take International Paper into areas of modest growth, higher profits and lower cyclicality. The big move came with his \$1.1bn purchase of Hammermill Paper in 1986. This gave International Paper a line of well-known fine papers and a superb mill at Riverdale near Selma, Alabama.

The company is trying to develop proprietary products in its bleached paperboard business, which is growing handily because of the increasing use of cartons by the drinks industry.



And in 1987, it bought the Antec photographic papers business in the US (for \$384m). It then added a manufacturing base in Europe with the purchase of the Hford division of Ciba-Geigy in the UK last year. This is a slow-growth business but relatively predictable.

Most important, International Paper spent \$320m on the French paper company, Aussedat Rey, earlier this year and will spend a further \$300m to develop pulp-making capacity to turn the company's Sallat plant into an integrated mill.

In a European market where barriers to trade seem to be falling like ninepins, Mr Georges

believes that Sallat could be in a powerful position as "the lowest-cost mill on the continent."

But Wall Street is so fixated on the prospects of a price slump that it is not listening. For International Paper to increase its value, Mr Georges must show he can take the company through next year's weak market without disaster.

Nobody knows this better than he. "My own guess is that by mid-1990, we'll see a stabilisation and an upturn," he says. "That will help the company, because it will demonstrate to all those doubters in the financial community that we can weather a downturn."

## Distance lends distortion to the view

A story that made us laugh like anything when I was at school concerned a man who was kidding himself out to go elephant hunting. He went to the Army and Navy stores and ordered a powerful telescope and a pair of tweezers.

"Certainly, Sir," said the shopman; "but I wonder if I could ask you to tell me how these will help to hunt elephants."

"It's quite simple," said the huntsman. "I'll carry an empty matchbox, of course. Then I'll sit in a tree until I see an elephant, look at him through the wrong end of the telescope, pick him up with the tweezers and pop him in the box."

I had forgotten this story years ago, but for some reason it has come bubbling insistently back to the surface while I was wading through the new OECD report on the US economy - an experience a little like swimming in heavy treacle. There is no direct parallel, but enough disregard for the obvious, misplaced ingenuity and plain nonsense to kick the subconscious awake.

The policy recommendations amount to saying that it would be a good idea to stick to present policies unless it proves advisable to change them, and can

safely be ignored. The interest is clearly intended to lie in the analytic chapters addressing such questions as competitiveness and industrial policy, productivity, tax incentives, and deregulation and its effects. There is some interest here, but not always of the kind intended.

Competitiveness interests the Americans to the point of obsession, but it is not very helpful for the OECD to join in the popular sport of drawing up league tables. Thus there are some agencies in the US exploring the fact that the US share of world output is much bigger than its share of exports, which goes into such details as continued use of the inch scale, and the diversion of research effort into defence.

The right comparison would not be with Japan or Germany but, say, with the EC as a single unit. This would have the same share of output as the member countries do in sum, but a much

smaller share of world exports, since all the exports inside the community would no longer count. This is part of a section on microeconomics, and supports my prejudices that a microeconomist is often a man who cannot see the wood for the trees.

Again, there is an occasional discussion of productivity. The US, like Britain, has enjoyed a jump in productivity during the 1980s, and probably for rather similar reasons. The OECD is worried because it cannot explain this change in detail, and even wonders if it has happened at all. "This doubt, it emerges from an appendix, is based on a plain howler. The trouble is that the tremendous improvement in the design and speed of computers has changed the way in which we measure productivity. As many Americans have pointed out in the past, today's lap-top will do the work of a roomful of heavy equipment 20 years ago, but the manufacturing problem is totally different, something that changes in detail, and even improves in efficiency, which is essentially a linear process.

So far, so good; but the OECD goes on to worry about the index number problem and reaches a wrong conclusion. When a rapid increase in efficiency enables pro-

ducers to cut prices heavily, it becomes hard to compare the level of output in two periods, since this is normally done at constant prices. This produces a startling result with computers: the share of computer output in total US manufacturing this year is four times higher when measured at 1982 prices as at current prices. "Conversely," the appendix goes on, "it is underweighted prior to the base year. Productivity growth is thus biased downwards before the base year and upwards thereafter. The productivity pick-up may therefore be an artefact of the choice of base year."

This is just plain nonsense. The effect of the weighting problem is to "overstate" growth both before and after the base year, as next to none of us far either of a moment's thought will show. This whole discussion is an artefact of muddled thinking, and distracts attention from problems. How, for example, to you measure computer output? (The US Census Bureau measures it in megaflops, or operations per microsecond, for want of a better unit, but this begs all sorts of questions). How, for that matter, do you measure output of services except in man-hours? And if these questions get vague or tan-

tological answers, do you know what you mean by productivity? Or, for that matter, by inflation?

One can understand the OECD being a little evasive on these basics, since if the numbers are questioned, so is its entire world; but this does not explain a discussion of leveraged buy-outs which fails to mention bankruptcies, and concludes that they may help efficiency by making investment decisions more responsive to the market and by removing these decisions from the influence of fund managers.

One suspects a bias in favour of deregulation. Equally, the OECD should surely face some of the big questions which are now actively discussed in the US. There is much talk of "progress" in "eliminating imbalances", but next to none of how far either of the twin deficits actually matter in the larger scheme of things. Americans, who have now noticed that the promised crisis keep failing to happen, are beginning to wonder. Of course there are true and helpful things in the report, and some startling facts - for example, that debt service peaked as a proportion of total US public spending five years ago, contrary to most popular rhetoric.



By Anthony Harris in Washington

But this is not enough to disarm my suspicion that the OECD, like any bureaucracy, tends to over-estimate the importance of government policy, and still more the importance of various arbitrary norms which are stated as policy objectives. Yet the real long-term problems of infrastructure and human capital do not get the attention they deserve and demand.

So there you have the view of the OECD in Paris as seen from Washington. It remains only to pick it up with my tweezers, and pop it into a matchbox.

## Economics Notebook

### Divergent views on unity

While there seems to be a good chance that next month's European Community summit in Strasbourg will set up an inter-governmental conference to discuss a new Treaty charting the course towards Economic and Monetary Union, it is equally likely that several heads of government will have some reservations about the enterprise they are launching.

Mrs Thatcher, the British Prime Minister, of course, apparently stands alone with her ideological objections to further transfer of economic sovereignty to the Community. Some other leaders ready to accept the principle will, nonetheless, be wondering whether the Community should take on such a difficult task when a great deal of attention must be given to developing its relationship with the "new" Eastern Europe. Others may be worried about the implications of it all, at least as they have been set out in the Delors Report.

Mr Karl Otto Pöhl, president of the West German Bundesbank, appeared to be counting on such misgivings during an interview on BBC television eight days ago when he doubted that many European governments would be prepared to accept West Germany's terms for creating a European Central Bank.

Bonn would naturally insist that the ECB be statutorily independent, as is the Bundesbank, and that its dedicated priority must be to contain inflation to an absolute minimum. Mr Pöhl was clearly against rushing towards EMU, preferring, instead, a two-year waiting period to allow completion of the European Monetary System and some of experience of living with a free capital movement regime.

work would begin under the chairmanship of Italy which has no shortage of thinkers on the subject in the Treasury, the central bank. Unlike some of the nation's politicians, they are by no means romantic dreamers, but people who are convinced that several practical economic and political reasons that the achievements of the single market cannot be preserved without clearly defining the EMU objective and steadily moving towards it.

One aspect which the British government would do well to ponder is that their political premise is wrapped in anxieties about sovereignty. Rather than sharing Mrs Thatcher's worries about losing it, these Italians want to clarify some differences between member countries. But the Italians believe it will not do for the future, for both political and economic reasons. Mr Carlo Azeglio Ciampi, governor of the Bank of Italy, apparently sent Mr Pöhl's eyebrows well up into his hairline when he bluntly stated some of these views at an Italo-German Forum last month.

The Governor duly played the sovereignty card - without ever using the word as part of a reasoned argument against Mr Pöhl's preference for leaving the DM as the EMS anchor currency. He reminded his audience that the building

of the Community is founded on "the basic principle of parity," and argued that as it is currently structured, the EMS is working contrary to this system. If it continues, warned Mr Ciampi, it would "create tension between member states."

Italian monetary officials are irritated by frequent Bundesbank claims that Italy would be one of the countries looking for a European monetary policy aligned on average inflation. Having already clearly indicated their support for an independent European central bank committed to price stability, they are looking for participation in policy-making rather than a higher inflation rate in West Germany.

The Italian central bank believes that the conditions which have established the DM as an anchor currency in the EMS - wide inflation differentials among member countries and capital controls in many - are being eroded and that in any case the dominance of an anchor currency conflicts with the principle of joint participation in the making of monetary policy which ought to underpin a monetary union.

Above all, Mr Ciampi and his colleagues argue that beginning work on an EMU treaty is a necessary concomitant of stage one of Delors. This will confer a wider role in co-ordinating monetary policies on the Committee of Governors which is also to be equipped with its own expert secretariat. But Rome believes that the Committee will need a framework of longer-term EMU objectives in which to operate. "We can be flexible about when we will arrive there, and about how we will arrive there, but we need to know where we are going," says a very senior official at the Italian central bank.

John Wyles

## THIS WEEK

THIS WEEK is dominated by US statistics. Of greatest importance will be Friday's Purchasing Managers' Survey for November, which is increasingly regarded as one of the most informative indicators of US economic activity. As the first US data from November it will offer the most up-to-date view of trends in manufacturing industry.

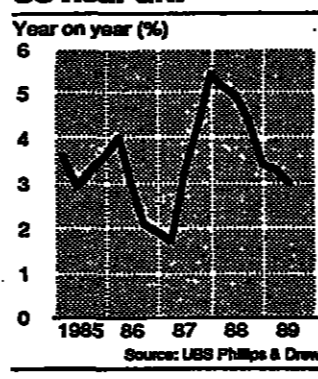
The survey is expected to provide further proof of how quickly the US economy is losing momentum. Analysts predict that the wide range of information in the survey on production, commodity price inflation, orders, and employment should reveal how much manufacturing industry has shrunk under the weight of an unfavourable exchange rate.

Preliminary figures for the US gross national product in the third quarter are out on Wednesday. They should complete the picture of a sluggish US economy. The consensus of analysts' forecasts, compiled by MMS International, the financial consultants, is for GNP growth of 3.6 per cent between July and September, compared with 2.3 per cent in the second quarter.

If these sets of statistics confirm the slowdown in the US economy, the Federal Reserve may decide it has room to loosen the bindings of monetary policy. The Fed is concerned that the economy may be decelerating too fast, and appears prepared to ease off the monetary brakes to stimulate economic activity. A cut in the key discount rate is possible, and economists are predicting that the Fed funds rate, currently about 8 per cent, will be at 8 per cent by the year end.

A quiet week for UK economic news kicks off today with the appearance Mr Norman Lamont, Chief Secretary to the Treasury, before the Treasury and Civil Service Committee. He is expected to be given a tough grilling on the Government's spending plans and forecast for the econ-

## US Real GNP



## "I wonder if he understood a word I said"

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INTERNATIONAL CAPITAL MARKETS

INTERNATIONAL BONDS

Private placements keep managers on the gravy train

WHEN SYNDICATE managers look back over 1989, they are likely to remember in snapshots the public events and issues that have dominated the year.

opacity and tardiness. So how tough has business actually been? Everyone in the Euro market agrees there are too many banks chasing too little business and that it has been hard to make money.

depends for its lenders largely (roughly 80 per cent, say the banks) on Tokyo. It generally involves more structured finance than the public market, and it uses little of banks' precious capital for underwriting.

ratio on an average private placement was higher than that of a typical public Japanese equity warrant issue, although he added that many deals are done without fees, the profits coming from arbitrage or swap activity.

Lynch do a remarkable proportion of the invisible business, largely off the back of their ability to create financial packages that suit borrowers and investors. Ironically, they are assisted in this by the tenacity of Japanese banks and securities houses not to compete so avidly where there is little publicity at stake.

Finally, 1989 has seen the rapid expansion of deals linked to equity indices. These are bought by a wide range of institutions and have been mainly for bank names.

INTERNATIONAL LOANS

A glimmer of life in Third World finance

THREE TRANSACTIONS emerged last week to show that international banks have not completely halted lending to developing countries, in spite of the lingering effects of the Third World debt crisis.

on delivery at \$71.5m. Underlying it all is political risk insurance, under which Lloyd's of London will cover for the possibility that the aircraft is not recoverable.

NEW INTERNATIONAL BOND ISSUES

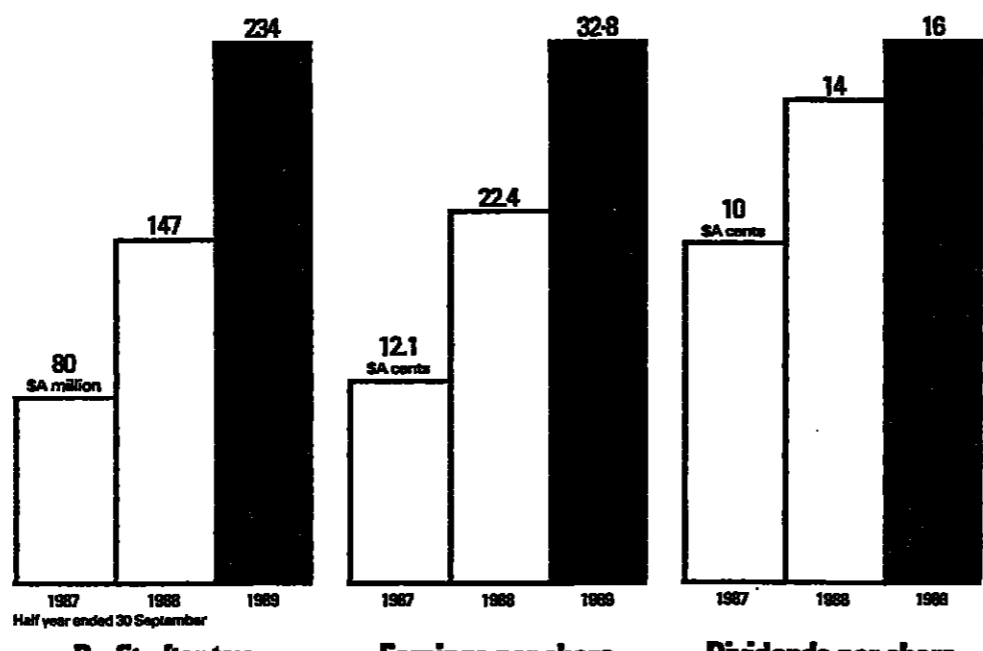
Table with columns: Borrowers, Amount m., Maturity, Av. life years, Coupon %, Price, Book runner, Offer yield %, and a second set of columns for another group of borrowers.

EUROMARKET TURNOVER (\$m)

Table showing Euro Market Turnover with columns for currency, month, and turnover values.

CSR maintains growth Half year 1989 results

Profits again grew strongly All businesses performed well



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Further details on CSR's results and growth prospects will be in the half-yearly results summary to be released on 22 December, 1989.

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November 1989

INTERNATIONAL CAPITAL MARKETS

US MONEY AND CREDIT

Fiscal policy regains centre stage

THERE WERE two interesting developments last week in the context of the most recent history of US economic policy. Firstly, the US Federal Reserve again moved, slightly ahead of the market's thinking curve, to loosen control on credit. This was in spite of a rather discouraging 0.5 per cent increase in US consumer prices in October, even after leaving out food and energy.

October was due to one-time price rises in particular materials such as cars, clothes and hotels. By contrast, forward-looking indicators point to sluggish economic expansion with both orders and shipments of durable goods depressed last month, according to last week's figures.

Mr Robert Brusca, chief economist at Nikko Securities in New York, believes the factory sector is weak across the board with orders and shipments down last month in primary metals, non-electrical and electrical machinery.

"Most firms continue to cannibalise their order books to maintain shipments at a weak pace; this cannot last for long. The Fed is certain to respond to these new signs - and that will keep the economy from recession," writes Mr Brusca in his weekly comment.

What Salomon Brothers calls a "deepening profits recession" - the product of mounting costs colliding with softening pricing and demand - is heightening business caution and limiting employment and capital spending growth.

The timing of the Fed's latest move during Thanksgiving week was not widely expected in spite of reports of pre-Christmas retail sales being disappointing as the consumer retrenches.

One theory was that the Fed wanted to encourage the leading money centre banks finally to lower their prime lending rates. After the last loosening move, only the ubiquitous Southwest Bank of St Louis and two other small banks lowered prime to 10 per cent from 10.5 per cent.

Mr Brian Fabbri, chief economist at Midland Montagu notes that, as the prime rate is cur-

rently around 240 basis points above competing 90-day commercial paper rates and 220 basis points above domestic CD rates, it should fall imminently. He also notes that banks and other lenders have been slow to lower mortgage rates.

Given the woes in some parts of the housing sector, the Fed probably wanted to encourage the other banks to follow suit, so sending an encouraging signal to the consumer.

What is probably more significant is that last week bore witness to the "world peace rally." Bonds rose briefly on news of US defence cuts in response to the melting of the Cold War. The Administration decided to request authority for steadily declining inflation-adjusted spending in 1991 to 1994.

In the same week, eager to get away for the Thanksgiving holiday, Congress passed, with less bluster than usual, a \$17.8bn deficit reduction package.

"The measure's effective fiscal restraint is greatly exaggerated by accelerated tax collections, dubious accounting practices and optimistic estimates of tax-base broadeners," Salomon Brothers noted. "But the continuation through Janu-

ary of across-the-board spending cuts, which will cumulate over subsequent years, provides genuine budget restraint."

Under persistent pressure from the Administration to ease monetary policy all year, the Fed has always said that the fiscal position would have to be tightened before any joy would be forthcoming from the central bank. Nobody ever anticipated any serious movement on the deficit from Washington but Mr Mikhail Gorbachev and the people of Poland and East Germany have done Capitol Hill an enormous favour.

Although the immediate effect in currency markets of the thrilling events in Eastern Europe has been to put the dollar under pressure against the surging D-Mark, cut in military spending and the other developments on the fiscal front should eventually help the dollar.

Treasury bonds did mildly well last week, particularly in response to the Fed's monetary easing. The need to offset recent hints of fiscal rectitude may induce a further move towards accommodation, something the bond market to look forward to.

Janet Bush

US MONEY MARKET RATES (%)

Table with columns: Rate, 1 week, 4 wk, 12-month, 12-month Low. Rows include Fed Funds (weekly average), Three-month Treasury bill, etc.

US BOND PRICES AND YIELDS (%)

Table with columns: Price, Change, Yield, 1 week, 4 wk. Rows include 5-year Treasury, 10-year Treasury, etc.

Money supply: In the week ended November 13 MI fell \$1.5bn to \$785bn.

NRI TOKYO BOND INDEX

Table with columns: Average, 12 m, 24 m, 36 m. Rows include Overall, Government Bonds, Municipal Bonds, etc.

UK GILTS

Interpreting the words of Major

THIS AFTERNOON, Mr Norman Lamont, the Chief Secretary to the Treasury, appears before the House of Commons Treasury and the Civil Service select committee to answer questions on the Autumn Statement.

Having spent lunch hours preparing responses to likely questions on the details of the Government's public spending plans, inflation and interest rates, Mr Lamont and his officials could well face questions on the predicted fall in the public-sector debt repayment (PSDR).

In his Autumn Statement, Mr Major revised the 1989-90 PSDR down to £12.5bn from £13.5bn. This compares with the £13.5bn predicted in Mr Nigel Lawson's March Budget.

This revision caused a ripple in the market, though Mr Lawson had earlier warned of a fall in the PSDR this time round. Until the Autumn Statement, continued repayment of debt on the same large scale was expected.

This is the biggest factor in the reduction in the size of the gilts market, which has been contracting by more than £12bn a year since 1983. Taking the smaller PSDR together with the £5bn more-than-expected public-spending forecast, the Chancellor had outlined what appeared to be a healthy recipe to propel the gilts market into the 1990s.

At last, market makers could say, the prospect of the Bank issuing gilts again to finance

expenditure plans was back on the horizon. Perhaps when the PSDR had diminished to a £7bn level.

After the statement, the ever-shrinking group of market makers in gilts (27 after Big Bang in 1986, now 19) took hope that they might once again outnumber gilts analysts - who have taken to calling themselves "staring board analysts" because gilts were scarce trading volumes sometimes negligible.

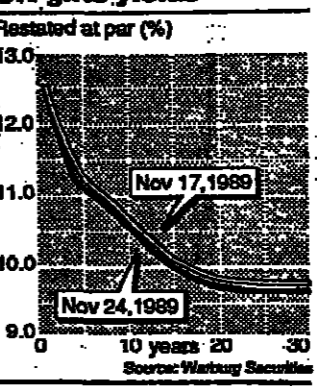
With a borrowing requirement rather than a debt repayment resulting in more gilts, long yields could rise to 11 per cent or more.

Gilt prices would come down with the yield of gilts, as they did in immediate response to the news in the Autumn Statement. Then bonds would become more attractive to the investment institutions needing a safe haven in which to match long-term liabilities and assets.

However, the Autumn Statement may have been too rosy interpreted too soon. Economists are not unanimous in their interpretations of how much the gilt market will contract. Funding arithmetic and economic forecasting bring a varied selection of estimates.

Midland Montagu is predicting a "considerable shrinkage" of £40bn in the market's present size of £220bn to £200bn by March 1991. This is arrived at by assuming a PSDR of £15bn in 1989-90 and 1990-91, which is

UK gilts yields



whether the Government will exploit the new funding rules. But assuming the Bank buys in £4bn worth of gilts in 1989-90 to sterilise intervention, the gilts market could contract by about £13bn next year, Warburg estimates.

At UBS Phillips and Drew and NatWest Gilts, the economists are also looking for the market to show a contraction of around £14bn by March 1990. On this trend, the market size could be £100bn by the end of March 1991.

All these assessments take the shine off the Autumn Statement for market makers in gilts. The continuing predicted reduction in market size over a two-year period, will, economists agree, considerably reduce the market's liquidity.

Even though the Bank is making efforts to improve liquidity with its already announced stock conversion programme, investors are still likely to be strongly tempted to invest in sterling corporate bonds instead of gilts. The Bank is accordingly very keen to see the rapid expansion of the sterling bond market continue to take up the slack.

But while encouraging the growth of parallel markets, the Bank is giving precious little away about the likely size of the gilts market over the next couple of years. If the market shrinks too quickly, the Bank has indicated that it "will take a view."

Rachel Johnson

CBT tightens price limits

THE CHICAGO Board of Trade is to tighten circuit breakers for its Major Market Index stock index futures contract, in a further move to curb stock market volatility, Reuter reports. The CBT has added

another price limit layer after a 30-point MMI fall and has narrowed the maximum daily MMI move to 50 points from 60. The proposed CBT changes are its second such move since the October 13 mini-crash.

Advertisement for MANUFACTURERS HANOVER, featuring various international bank services and branches. Includes logos for MPS, Banca CRT, Banca Anafoli, and others. Text: "A Driving Force in Italy".

FT/IBD INTERNATIONAL BOND SERVICE

Large table listing international bond services with columns for Country, Bond Name, Maturity, Yield, and Price. Includes entries for USA, Canada, UK, France, Germany, etc.

STRAIGHT BONDS: Yield to redemption of the mid-price. Amount listed is expressed in millions of currency units except for Yen bonds, where it is in billions. WARRANTS: Daily warrant price - source premium over current share price. Bond warrant at 21¢ - exercise yield at current warrant price. Coupon prices on 24th Nov 1989.



INTERNATIONAL CAPITAL MARKETS AND COMPANIES

# Rate increases hit Japanese banks

By Stefan Wagstyl in Tokyo

JAPANESE BANKS' profits have been squeezed by rising interest rates, forcing some of them to announce their first reductions in interim net profits since 1981, the year they started reporting interim figures.

The increases in interest rates pushed up the cost of money at a time when the proportion of funds raised at market rates, as opposed to artificially low regulated rates, is rising rapidly due to liberalisation.

The banks have been hit hard by the fact that short-term rates, at which they often raise funds, have risen further than long-term rates, the rates at which much of their money is lent out.

The total net profits of the 12 leading city (commercial) banks plus the Bank of Tokyo, which reported unconsolidated results on Friday, rose just 2.3 per cent in the six months to the end of September.

The biggest five reported declines in net income. For the full year the 13 banks expect reductions in net income following further increases in interest rates and likely write-offs on loans to Mexico.

The banks were unable to cover up their difficulties to the same extent as in the past by selling large amounts of securities because the Ministry of Finance has urged self-restraint and ordered accounts to be presented in a more transparent way.

For the first time, the banks have had to reveal a new category of profit - called net operating profit - which excludes profits from capital gains on most kinds of securities. As the table shows, net operating profits are considerably lower than pre-tax profits,

	Pre-tax profit	% chg.	Net op. profit	% chg.	Int. income	% chg.	Net profit	% chg.
DAI	144.6	+3.8	88.9	+12.0	38.4	+2.8	80.3	-3.1
Sumitomo	190.7	-2.2	145.0	+88.2	67.3	+11.3	87.1	-1.1
Fuji	147.1	-12.7	108.9	+7.3	46.3	+25.8	33.8	-1.1
Mitsubishi	170.4	+3.3	85.7	-33.8	33.5	-14.2	80.4	-2.0
Sanwa	171.5	+8.0	127.0	+58.6	52.9	+55.5	50.2	-0.1
Total	77.0	+13.0	37.2	-34.8	25.0	+23.5	34.9	+15.0
Mizuho	69.4	-0.3	15.4	-82.4	20.6	+26.3	23.5	-1.2
Tokai	58.5	+12.7	44.9	+14.7	15.8	+24.5	30.8	+19.2
Daiwa Bank	47.5	+8.0	47.7	+9.8	7.9	-27.2	24.9	+32.7
Kyowa	43.8	-2.7	37.0	+2.8	7.0	+6.8	20.4	+5.6
Saitama	34.5	+1.8	30.5	+8.5	10.3	+40.5	18.3	+19.9
Hokkaido	24.4	+25.7	18.7	+8.7	6.7	-18.1	11.3	+31.7
B of Tokyo	48.4	-3.5	42.4	-8.5	78.9	+11.1	32.7	+3.0
TOTAL	1229.9	+1.8	830.9	+2.9	406.6	+14.2	626.7	+2.8

which, in the traditional way, include gains on securities transactions.

The most startling revelation is the particularly heavy reliance on securities profits of Tokyo banks - including Dai-ichi Kangyo Bank, Mitsubishi Bank and Sanwa Bank - in comparison with their fast-growing rivals from Osaka - Sumitomo and Sanwa. Mitsubishi's net operating profit is only half the pre-tax figure.

Sumitomo is by far the most profitable bank at both the net operating and the pre-tax level, as before.

Sanwa shot up the profits' table from fourth position to second, overtaking Fuji Bank and Mizuho.

The Bank of Tokyo, which once dominated foreign exchange business, has kept its traditional lead in revenues from international operations. Sumitomo was second and Mitsubishi third. Sanwa, with a 35 per cent increase, jumped ahead of DKB and Fuji into fourth position.

A prolonged decline in the Japanese bond market this year hit the banks' bond dealing profits, normally a useful source of supplementary revenues. Combined bond dealing profits dropped 38.4 per cent to ¥14.9bn (\$104m). Fuji reported its first-ever loss from bond dealing - ¥4.5bn. The Bank of Tokyo made a profit on bond dealing after a loss for the same period last year.

# Swedish group buys St-Gobain filters arm

By George Graham in Paris

CAMFIL, a privately-owned Swedish filtration company, is to buy Soflira-Poelmann, the industrial filters subsidiary of St-Gobain, the leading French glass and pipes group.

The acquisition will, according to Camfil, create the leading European industrial air filtration group, with combined sales of around FF7750m (\$122m) and a solid presence throughout Europe.

Mr Jan Erik Larsen, Camfil's president, said the two companies were highly complementary, with Soflira mostly present in France supplying clean rooms to users in the fields of nuclear energy, hospitals and electronics. Camfil is more active in general filtration, with production sites in Sweden, West Germany, Switzerland and Ireland.

Mr Larsen said the air filtration market was expanding steadily, with strong demand from the electronics industry for clean rooms, but was not booming because of the increased enthusiasm for environmental protection, as some imagined.

Soflira, which made net profits of FF122m last year, is 72 per cent owned by St-Gobain, with the remaining 28 per cent held by Soudure Antigonish Francaise, a subsidiary of the Air Liquide industrial gases group.

Mr Larsen, whose group was advised by the Enskilda investment bank for the transaction, refused to disclose how much Camfil had paid, but said it represented a "fair market price."

# Enimont in limelight as Gardini guards his hand

By John Wyles in Rome

ENIMONT, the Italian public-private chemicals joint venture, looks set for a starring role on the Milan stock exchange this week because of serious doubts about whether Mr Baul Gardini's Montedison group ultimately intends to hang on to its 40 per cent stake.

Enimont shares rose 3.35 per cent to L1,470 last Friday after heavy trading, reflecting strong demand from London.

Investor interest was undoubtedly sparked by Thursday's statement from the Montedison board that "contractual relations between the two majority shareholders in Enimont must be the object of substantial, coherent modification to protect the interests of Montedison and of its shareholders."

As usual, Mr Gardini, whose Ferruzzi group controls Montedison's tax exposure on its capital gains from L1,100bn (\$877m) over five years to L270bn over the same period.

Not a man famed for his depths of patience, Mr Gardini's wrath finally exploded last week when the lower chamber of the Italian parliament succumbed to the blocking tactics which have bedevilled the Gov-

ernment's tax proposal for much of the year. The Montedison board warned on Thursday that parliament's failure to adopt the legislation by the end of the year "would remove one of the bases upon which Enimont was founded."

The company pointed out that at the end of its operating year it had to know about its tax treatment to prepare a set of accounts.

Signs of menace from Mr Gardini's direction have brought the instant reassurances from government ministers that every effort will be made to pass the necessary legislation in time.

This means that resistance will have to be quelled among politicians in the governing majority about using tax favours to encourage industrial restructuring during a race against time to push the legislation through both houses of parliament. These are not circumstances in which the Italian parliament always gives of its best.

# IBJ tumbles midway as rivals advance

By Ian Rodger in Tokyo

PROFITS OF Industrial Bank of Japan (IBJ), the largest of Japan's three wholesale banks, tumbled in the six months to September 30 because of the higher costs of raising capital.

The two other wholesale banks, Long Term Credit Bank of Japan and Nippon Credit Bank, both enjoyed very rapid profit growth because of highly-profitable dealings in foreign exchange and government bond markets.

Bank	Revenue	% chg.	Business profit	% chg.	Net income	% chg.
IBJ	1,288.1	+22.8	65.6	-28.7	51.1	-9.4
LTCB	891.5	+28.9	41.7	+236.2	36.4	+8.6
Nippon Credit Bank	546.4	+18.1	23.8	+211.0	22.3	+13.9

# IBCA promotes five to top AAA rating

By Stephen Fidler, Euromarkets Correspondent

IBCA, the London-based rating agency specialising in bank credit analysis, has promoted five Japanese banks to its top-rated AAA category.

This brings to 13 the number of international banks given IBCA's highest rating, a list from which Japanese banks were previously absent.

The banks added are Fuji

Bank, Industrial Bank of Japan, Mitsubishi Bank, Sanwa Bank and Sumitomo Bank.

IBCA cited the continuing strength of the Japanese economy and of the Japanese stock market, which have enabled Japanese banks to raise their capital ratios and to use some of their hidden reserves to maintain earnings.

"Credit-quality measures by

and large are very strong, and the Japanese banks well placed to pursue their policy of overseas expansion," IBCA said.

It said an important consideration in the ratings was the weight placed on the inherent strength of the Japanese system and the strong commitment of the Japanese authorities to the banks.

Standard and Poor's, the US rating agency, allots its AAA rating to only one bank, the Industrial Bank of Japan.

Moody's has five top-rated Japanese banks, similar to IBCA, except that it assigns Dai-ichi Kangyo, the largest bank in the world in terms of assets, a top rating and not Sanwa Bank.

# Mel Brooks to take film company public

BROOKSFILMS, a US film company headed by Mel Brooks, said it planned to go public through an initial offering of 1.5m units at a price of between \$9 and \$11 apiece, Reuters reports.

Each unit, according to an SEC filing, will consist of one share of common stock and one warrant to purchase one-third of a share of common stock.

# Australian bond buy-back plan

By Chris Sherwell in Sydney

THE Australian Government has unveiled details of its first reverse bond tender to retire federal government domestic debt, confirming its continuing withdrawal as a borrower and forcing a significant adjustment on the country's capital markets.

The reverse tender plan was first announced in the August budget, when Mr Paul Keating, the Federal Treasurer, foreshadowed a government surplus of A\$9.1bn (US\$7.1bn) for the financial year to June 1990. The tender, a mirror image of a conventional tender, will start on December 5 with an offer to repurchase about A\$150m in bonds.

An announcement said the Government would be seeking Treasury bonds of 13.0 per cent December 1991, 12.5 per cent May 1992, 13.0 per cent June 1993 and 13.0 per cent February 1995. But it would reject offers it does not consider sufficiently attractive,

even if this means the volume of repurchases is less than intended.

Although the repurchase is small, its significance is that it removes from the market government securities which the country's banks are obliged to hold to meet their liquidity ratios. With bank deposits generally rising, "it has all the makings of a squeeze," one investment banker said of the process.

The debt repurchases also raise important questions of monetary policy management for the Reserve Bank of Australia, the country's central bank. Mr Keating was reported to have said in London that the Australian Treasury bond market would end in three years, and to have indicated that a corporate bond market might replace it.

If this happens, the Australian Government would be breaking new ground internationally in the techniques of monetary management. But as

far as investment bankers are concerned, they are expecting strong growth in Australia's corporate bond market over the next few years anyway.

This is not only because of the emerging shortage of federal government stock, reinforced by a similar trend for semi-government stock. It is also the projected result of a rapid growth in pension funds following recent government superannuation reforms.

Investment bankers say the only home for large volumes of investible funds will be corporate bonds and asset-backed securities.

Currently Australia's corporate bond market has more than A\$5bn of securities on issue - a fast expansion since it began in 1987. But according to Dominguez Barry Samuel Montagu, a key player in the local market, institutional holdings of corporate bonds will increase dramatically to an estimated A\$17.5bn by 1992.

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UK COMPANY NEWS

BAT to take no action after advisers meeting

By Vanessa Houlder and Nikki Tait

BAT INDUSTRIES, the tobacco-based conglomerate which has been under bid threat from Sir James Goldsmith's Hoylake consortium...

lance or buy off Goldsmith". The meeting also covered the potential for "driving a wedge" between members of the Hoylake consortium...

following the leak of minutes taken at the meeting to Mr Jacob Rothschild, one of the Hoylake consortium's members...

Ferranti rescue plan by former chairman likely to fail

By Hugo Dixon

A PLAN by Mr Sebastian de Ferranti to mount a rescue package for Ferranti International Signal, the troubled defence electronics company...

British Airways, to lead the new management team. The idea was that Lord King would carry sufficient authority in the City so that funds could then be raised to plug the black hole that has appeared in Ferranti's balance sheet...

ranti's future because he is shortly due to take over as chairman of Smith New Court, the stockbrokers which acquired a substantial stake in Ferranti from Mr Jim Guarin, Ferranti's former deputy chairman...

groups that have registered an interest in buying Ferranti. In order to get access to information about Ferranti's operations GEC has had to sign a confidentiality agreement and it might therefore have been thought that any separate initiative by Mr de Ferranti posed a conflict of interest...

Ferranti directly because of its dominant position in the UK defence electronics market following the acquisition of Plessey earlier this year. However, GEC is believed to be anxious to prevent Ferranti falling into the hands of Thomson CSF, the French defence electronics company, and British Aerospace. These have formed a consortium to look at the possibility of acquiring Ferranti and are widely regarded as the front-runners to buy it, though it will be a couple of weeks before they decide whether to bid.

Shareholders with 40% of capital back Pearl

By Ray Bashford

MR EDINON HOLLAND, chairman of Pearl Group, said yesterday that he had received commitments from shareholders with over 40 per cent of the capital to oppose the £1.24bn takeover from Australian Mutual Provident...

Tootal chief says no to a lower Coats bid

Mr Geoffrey Maddrell, chief executive of Tootal, yesterday ruled out accepting a substantially lower price from Coats Vyeella, its fellow UK textile group, when it renews its bid. His statement followed a report that Coats, which already owns 30 per cent of Tootal, will pitch its bid at around 100p a share...

Mr Ian Byatt - Director General of Water Services to give him his full title - doesn't look like the sort of person who is going to misbehave. Nor is incapacity likely to be a problem for the 57-year-old former economics lecturer...

A watery issue: shareholders or consumers

Andrew Hill and William Hall analyse the problems facing the new regulator

THERE ARE two grounds for dismissing the new regulator of water: misbehaviour or incapacity. Mr Ian Byatt - Director General of Water Services to give him his full title - doesn't look like the sort of person who is going to misbehave...

solid returns for shareholders. And yet in spite of these apparent guarantees, Mr Byatt has already found himself at the centre of political and financial debate. Critics of privatisation have warned of the harmful effect a "hostile regulator" (hostile to the investor, that is) could have on the water companies' profits and dividends...

avoid the political limelight. The Labour Party, in particular, argues it will be able to change both the DG and his priorities if it gets into power. Mr Byatt is adamant about the DG's ability to resist political influence. "I do not answer to the Secretary of State for the Environment," he says. "I am responsible under the [Water] Act," he says...

concentrated on that rather than the highly political issues, such as the precise ownership of the industry." But the political debate extends beyond the fundamental pros and cons of privatisation. It includes worries about the so-called "cost pass-through" mechanism, which allows the DG to pass certain unexpected costs straight through to the water consumer in the form of higher charges...

As to what constitutes a reasonable rate of return, Mr Byatt says, "I do not have a figure in my head. I want to keep my eyes open and see what kinds of numbers begin to emerge from the City." This is characteristic of the flexibility of Mr Byatt's Birmingham-based office - "I genuinely want it to be an open system" - which he says will draw on the advice of merchant banks (on the cost of capital), of industrialists and of 10 customer service committees...

Robert Maxwell may bid for Monotype

Mr Robert Maxwell, publisher of Mirror Group Newspapers, is considering making an offer for Monotype Corporation, the typesetting equipment manufacturer which has agreed a \$250m bid from King, Black & Associates, a US investment group, writes Vanessa Houlder...

"may well be able" to bid for Monotype. "We are building an interest in the pre-press area. Monotype might fit in." King Black's offer was "significantly too low", he said. "As a shareholder we will not sell at this price."

remained below five per cent. Monotype's share price climbed from 110p to 155p. King Black, which provides technical support and capital to high technology companies has acceptances representing just three per cent of Monotype's shares. Its proposed deal with Monotype would be its first venture into the UK.

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# FINANCIAL TIMES SURVEY



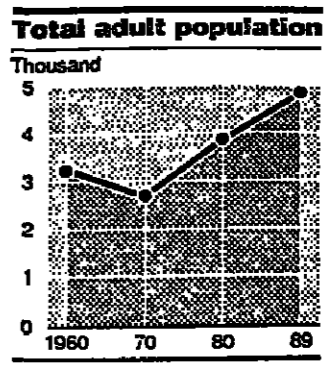
In the mid-80s, one of Britain's smallest Caribbean dependencies was rocked by political scandals. For the Nineties, the islands have pinned their economic future on offshore finance and tourism. Gordon Cram analyses the prospects in this survey.



## Turks and Caicos

Total revenue expected to flow into the Treasury during 1989/90 is \$44m, almost double the amount during 1988/89. Of this \$2.2m (\$139,000) is expected from company registrations and 1.7m (\$60,000) from tourist levies. This increased revenue has meant that the islands' economy has achieved a turnaround in the last year taking the dependency out of the most literal meaning of that word. Mr Oswald Skippings, Chief Minister, believes that investor confidence has been restored after the traumas of the mid-1980s. The economic outlook is discussed by Gordon Cram on Page 2.

**ON OTHER PAGES**  
Banking and finance and UK relations, Page 3; Tourism and communications links, Page 4; Industry and fisheries, Page 5.



KEY FACTS	
Area:	430 sq km
Population:	13,000 (est 1989)
	7,413 (1980 census)
	Economically active
	2,909 (1980 census)
Chief Minister:	Oswald Skippings
Currency:	US dollar

### Two-lane road to better times

MORE THAN 30 channels of satellite television reach the Turks and Caicos Islands; there is not one bookshop. Fisheries form its only productive industry, yet local hoteliers find it easier to serve lobster flown frozen from Miami. Wild donkeys meander the main street of Grand Turk, the capital, which is establishing itself as an offshore finance centre.

These are only the most visible of the contradictions which surround the islands, one of Britain's smallest and least developed Caribbean dependencies, as they enter the 1990s. The new decade offers a few avenues towards greater self-reliance. It should also leave behind a period when local politicians were discredited by scandal, and overseas investment - from resorts to reinsurance - was set back as a result.

Beneath the surface peculiarities of this tiny territory lie more enduring questions about its future. Although a better economic showing has just ended a reliance on the UK for an annual cash injection to balance its books, capital aid for development costs Britain at least \$5m a year and is this year being bumped up to nearly \$24m. And while economic independence is the goal both of London and of the colony's own elected leaders, political independence is by common consent at least 10 years off.

In the interim, British officials will have to maintain their patrol of a local political arena which, in spite of a two-year suspension of elective government from 1986 and a change in ruling party, is still pitted by allegations of patronage and cronyism.

The Turks and Caicos nestle at the south-eastern end of the Bahamas chain, with which they were federated for most of the last century. Their less than 200 square miles of flat, scrub-like land area is spread among some 40 islands and smaller islets, or cays - hence one part of the territory's exotic name, given by early Spanish explorers. The other comes from the fez-like red flower on the Turk's Head cactus, which grows determinedly in its otherwise inhospitable soil.

A population of about 13,000 is concentrated on six main islands, but their number is said to be matched, if not doubled, by those who have moved away to seek the employment which they are unable to find at home. Some of these, like

construction workers in the Bahamas, will in a pity TCI saying he "boiling two pots" - temporarily living abroad while sending money to the family they have left behind. Others, particularly the brightest who have turned to a US college for the tertiary education which is also unavailable locally, are gone for good.

Hopes of advancement for the islands lie in two main directions. One is offshore finance, a business developed in Grand Turk during the 1980s by small firms of largely expatriate lawyers, bankers and accountants attracted by the absence of tax and the TCI's use of the US dollar as its currency. The financial sector is now to be put on a more regular footing with a package of legislation intended to be in place by the end of the year.

From the islanders' point of view the industry will never be a mass-scale employer, while the professionals who are its motive force will need to assess in what areas they can best compete against more established jurisdictions in the Caribbean and elsewhere. At the same time, the newly enunciated regulators have a delicate job in keeping things clean - but not throwing the baby out with the bathwater.

The other way forward for the TCI is in tourism. Its impact, negligible at the beginning of the 1980s, has already transformed Providenciales, the westernmost inhabited island and known as Provo, since club Méditerranée picked it as the site for a holiday vil-

lage which opened five years ago.

As if in recompense for their unappealing inland vegetation, the islands have been blessed with spectacular coastlines of pale, fine sand. A narrow range of temperatures around the mid-80s and low humidity also help.

With coral reefs giving way to a sheer ocean wall, the TCI is regularly ranked by diving enthusiasts as one of the world's top five locations - a specialist market which helps even the spread of business outside the peak winter vacation months.

While Grand Turk remains a village, Provo has become a full-blown resort, with new hotels opening each year. It has also brought soaring prices for residential land, and Provo is enthusiastically described by the largely American property investors there as "the new Grand Cayman". But an adequate secondary market for housing has yet to emerge, and a standard 30 per cent discount which developers offer to those with TCI resident status suggests that asking prices may be somewhat inflated.

The growth of Provo has not been without its problems. Labour has drifted there from the other islands, but jobs in the tourism business are often seasonal and sporadic, and construction projects have been prone to lengthy delays. An attempt is being made to restart work on a half-built Sheraton, while a Ramada hotel is due to open next year, also behind schedule.

Mr Oswald Skippings, the islands' Chief Minister, believes such troubles are now over, and sees a restoration of investor confidence after the trauma of 1985 when Mr Norman Saunders, his predecessor but one, was arrested in Miami and convicted on charges involving the receipt of drug-related funds.

Mr Skippings is happy with the level of development activity taking place but is concerned that it is concentrated on Provo - where he says saturation will be reached "only a few years down the road" - and that not enough is being done to pass on to islanders the skills in building and management which the projects require.

"I am sure the private sector will inevitably play the leading role in terms of bringing about the infrastructural change that we need to undertake," he said. But he added: "It is not our intention to let development take place around us. Our people must be participants, must be involved. If they are not qualified to participate then they have to be trained, and that is also one of the areas where we request the investors to assist."

The People's Democratic Movement (PDM) led by Mr Skippings came to power in March last year for the first

time since 1980. Its landslide victory, taking 11 out of the 13 elected seats in the Legislative Council, came in spite of British constitutional attempts to provide a more diverse range of voices in the islands' assembly. In the two-party system which has emerged in the TCI, support for the government of the day has often been rewarded with individual favours, while those loyal to the opposition have been commonly excluded from jobs, public sector contracts, and allocations of Crown land.

Political strife reached its height under the Progressive National Party (PNP) administration in the months following Mr Saunders' arrest. It led to a commission of inquiry conducted by Mr Louis Bloom-Cooper, the British barrister. His report reads like a tropical thriller, with chapter headings such as "Corruption at the cemetery wall" and it accords a key role to Mr Skippings, the then Leader of the Opposition, against whom he found "a strong prima-facie case... for incitement to commit acts of violence".

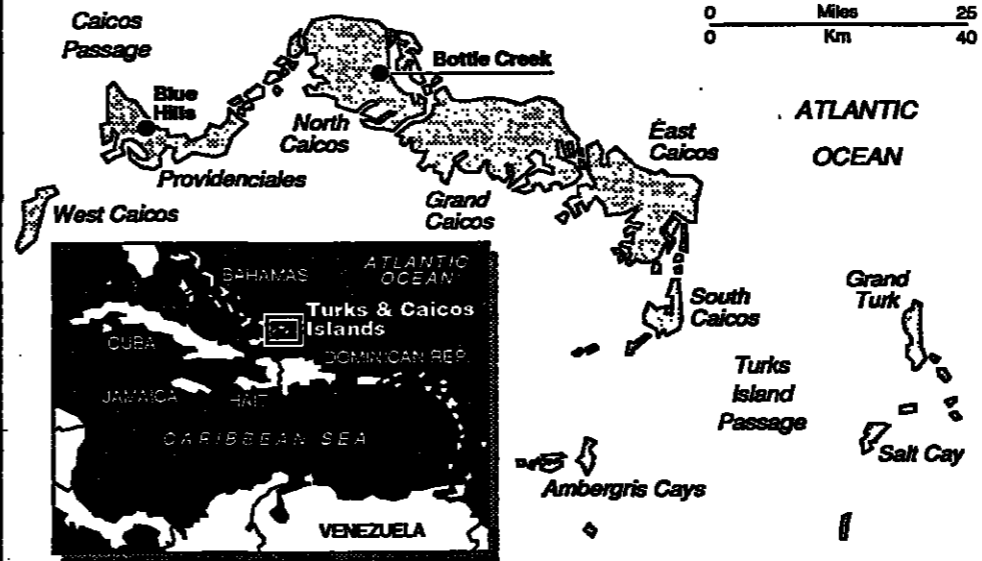
The episode, involving the New Year's Eve arson of a government building in Grand Turk, did not prompt criminal charges, and the commission held that he and the PDM "must not be deprived, or appear to be deprived, of any opportunity to become the elected members of the Turks and Caicos Islands Government".

And so it was. Mr Skippings, once the West's youngest head of government, is still only 36 and, when asked to reflect on his role in the upheaval, denied violent intent but acknowledged: "We get older, we get wiser."

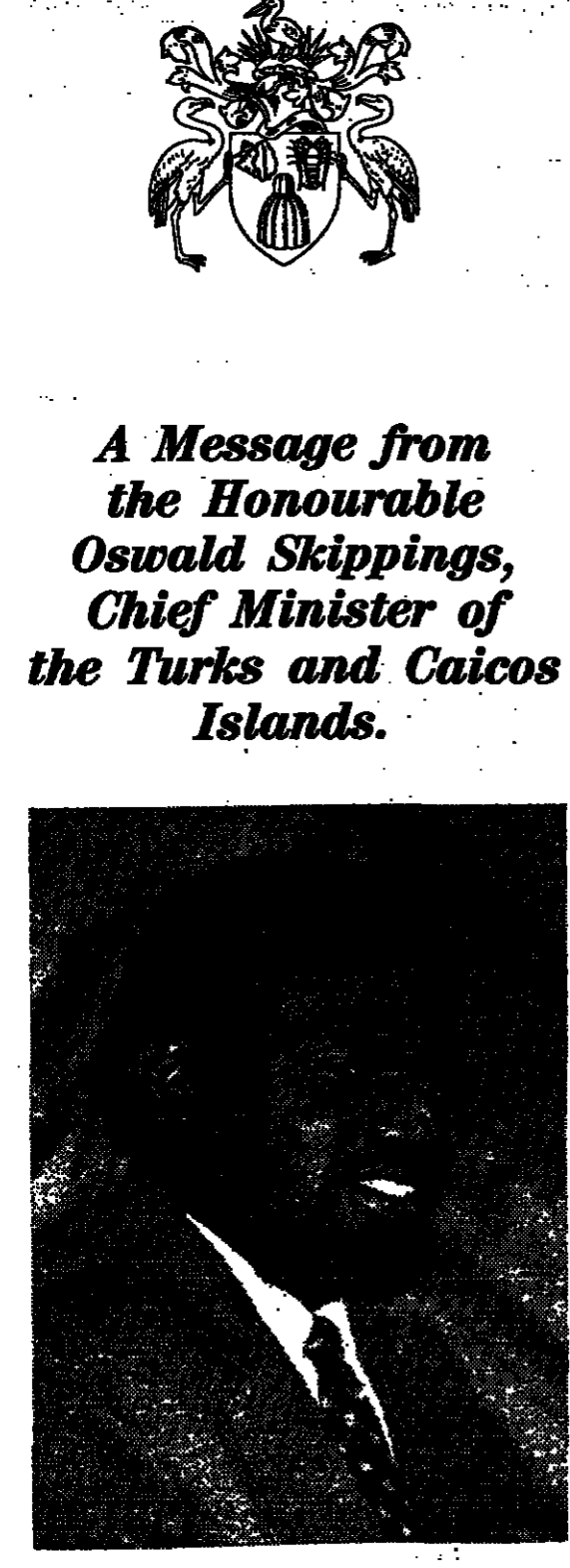
Although the UK is now exercising tighter financial controls, independent observers of the political process in Grand Turk believe that territory has some way to go before it will be rid of abuses, and the PNP contends that little has changed except the party in power.

Mr Alden Durham, Leader of the Opposition, admits of his party's own last period in office, "We really messed up."

Continued on Page 2



### ADVERTISEMENT



**A Message from the Honourable Oswald Skippings, Chief Minister of the Turks and Caicos Islands.**

In this my second year in office, I am happy to participate in this survey on the Turks and Caicos Islands.

We are a government that understands its responsibilities to develop the economy, to provide a better standard of living for all our citizens, and to create a new upward mobility for our population as skilled financial services and professional workers.

Our long term goal is to develop our financial services industry to the stage where these islands are considered the foremost corporate domicile in the region. For this to happen, it is imperative that we develop a reputation for integrity and high standards of professional conduct.

This combined with financial freedom, investment privacy, absence of direct taxation and a growing financial services infrastructure of banks, insurance companies and trust institutions has already put us on the path to success. We hope that the international financial community will come to view our growing financial services industry as one which is safe and well protected by proper legislation and appropriate supervisory controls.

**REGULATORY AUTHORITY**

To achieve these aims we are implementing a partnership of the public and the private sectors through the establishment of a regulatory and promotional authority. This entity will represent the interests and concerns of the government, as well as the members of the local financial community and their offshore clients in areas of regulation, legislation, investor protection and promotion.

The Authority will promote the investment and financial opportunities of the Turks & Caicos Islands as an outpost of free enterprise and financial freedom in a world where private wealth and investment freedom is increasingly government controlled.

Proper regulation and supervision of a financial industry go hand in hand with promotion when the primary purpose of the increased regulation is to protect investors rather than to raise revenue. In those nations where direct taxation is a fact of economic life, government, the financial industry and the investing public tend to find themselves in an adversarial relationship, because regulation is used primarily to control and tax, and in some

extreme cases confiscate wealth. This is in direct contrast to the purpose of our supervisory regulation, which is to protect investors and enhance investment freedom and opportunities.

Important legislation has already been passed by our Legislature and awaiting assent. This will certainly enhance our offshore industry.

**RAPID AND RELIABLE SERVICE**

Our goal to become a "big player" in the international offshore market is quite a challenge. Countries such as Switzerland, Bermuda, Hong Kong and the Channel Islands all have a history and depth of expertise that we seek to develop over the coming decade. In the interim, with no legal requirement for Turks and Caicos companies to have resident directors or for the holding of meetings within the Islands, I see ourselves complementing these traditional jurisdictions by being able to provide an efficient, rapid, reliable and inexpensive service in corporate entities and trusts, the active management of which may be conducted in those centres where the infrastructure is already in place.

In previous years, Panama has been on of our traditional competitors in the area of simple and inexpensive companies to be used for personal asset holdings, investment, trading and the like. I am sure there are very few practitioners who are not aware of the events in Panama. With the very real possibility of that country becoming progressively less aligned with the Western democracies, we see enormous opportunities, and in fact we have already seen the shift in the significant increase in the rate of new incorporations.

So we turn to our direct competition, which we see as Gibraltar and the Isle of Man in Europe and British Virgin Islands in the Caribbean. In the corporate area, we offer a similar or identical product to those jurisdictions at the same or less cost and we are more efficient in terms of the time it takes to get names approved and incorporation documents processed. I do not think it is an exaggeration to say that a company cannot be incorporated any quicker than in the Turks and Caicos Islands.

It is also important to note that in contrast to those jurisdictions we are the only pure tax haven in that there are no direct taxes of any sort levied by our government. We offer a service in quick, easy and inexpensive asset holding and trading companies. We also offer confidentiality and investment freedom, not only in the area of companies but also in banking services and trusts. Eurodollar deposits are available through the

banks operating in the Islands. Without the need for exchange controls, funds can move in and out of the Islands freely without any of the usual formalities of seeking permission and/or disclosing beneficial ownership. I would hasten to point out that the banks adhere to strict internal policies and most professional firms have put their names to a Code of Conduct, all designed to deter as far as possible the unscrupulous, or worse, the criminal operator from using these Islands as a hide-away for ill-gotten gains.

Our insurance industry is also growing, particularly in the area of credit life re-insurance. End-users find that our fees for incorporation and other services are considerably lower than Cayman, the Channel Islands or Gibraltar.

**TOURISM GROWTH**

Regarding our second growth sector, tourism, we are in the early stages of developing our tourist industry. Our climate, our beaches and crystal clear waters and our proximity both to major centres of population and to transportation hubs, all combine to virtually guarantee a successful tourism industry. Tourist arrivals for the first seven months of 1989 are up by some 38.2% over the same period last year.

The completion of the Ramada hotel and casino in early 1990 will complement the existing Club Med resort and Sheraton Hotel which is also in the course of being built. There is also plenty of room and scope for marina-type developments and a need for more intimate lodgings for the vacationer seeking tranquility and quaintness that is evident in Grand Turk and Salt Cay.

Efforts are being made to improve international air services to the Islands, which hopefully will offer additional flights to our existing services provided by Pan Am World Airways. Easy access to and from the islands is also vital to the development of our tourist industry.

With the help of HMG, an attempt is being made to further develop the potential of our fishing industry, on which the livelihood of a number of less developed islands continue to rely.

We believe that our Islands have the potential to become the Liechtenstein of the Western Hemisphere by the year 2000. Our advantages, combined with the right levels of regulation which impending legislation will bring to the financial industry, could propel this tiny nation ahead of Cayman as an investment haven for the over taxed and over regulated developed world. Our government will provide the stewardship, stability and integrity necessary to bring this about.

The Chief Minister's Office  
Grand Turk  
Turks and Caicos Islands

**TURKS and CAICOS 2**

**THE ECONOMY**

**Dependent no longer**

SMALL DOES not equal beautiful in the Turks and Caicos, although the islands themselves are both. Not only are government revenues inadequate to generate big infrastructural development from its own resources, but the economy can be swung pivotally by just one direct investment commitment from outside.

By the same token, the territory is exposed to any world downturn in tourism activity, which sustains many islanders. The TCI has been bereft of commercially-extracted natural resources since the salt industry collapsed in 1964. Since

then the colony has been left in an ultimate double-bind: on the one hand, there is little land which is both arable and served by freight transport to ship produce out, and there are no economies of scale to facilitate manufacturing for local consumption.

On the other hand, the resulting import dependence

means high prices - nearly everything, from milk to machinery, comes in through Miami. This, in turn, forces up wages.

The protection against adverse foreign exchange movements the islands gain by using the US dollar as their currency, is offset by the immediate cost disadvantage

which faces potential new industrial projects when compared with nearby low-pollution economies such as the Dominican Republic and Haiti.

Illegal migrants, who slip in notably from those two countries only 90 miles to the south, provide a further distorting influence, accounting for perhaps 10 per cent of the total non-tourist population.

But, it is acknowledged unofficially, they help the hotels business and basic services to function by their willingness to accept labouring and cleaning jobs which "belongs" often shun.

That is not to say all islanders are comfortably off. There are no official figures for average wages, but estimates range from \$100 a week upwards. Although poverty is not greatly in evidence, unemployment is conservatively estimated at 12 per cent, a picture which is certainly worse on some islands and which is exacerbated by the virtual absence of welfare benefits.

Nevertheless, the TCI economy has achieved a turnaround in the last year which is hailed alike by local politicians and London-appointed civil servants. It has brought the dependency out of the most literal meaning of that word - for several years at a stretch British funds were required as direct budgetary aid, merely to redress an annual and recurring excess of expenditure over incomes.

Budgetary aid, which reached a peak of \$3m in 1986-87 while the elected government was suspended, was eliminated by this April.

Other forms of financial support continue, through small amounts from the European community, Canada and the Caribbean Development Bank (CDB), as well as British capital aid where development grants are being nearly quadrupled in the current year to an exceptional \$23.8m from \$6.1m. Such support is common, though, to most of the UK's overseas territories, whereas the former yearly injection to balance the TCI government's books was both unusual and clearly a discomfort to Whitehall.

According to CDB estimates, growth in TCI gross domestic product, which hit a peak 29 per cent in 1985 just before the impact of that year's political turmoil, slipped back to single figures before rallying strongly last year for a rise on 1987 of 24.5 per cent. Total GDP for 1988 stood at \$63.1m.

The revival was assisted in delayed form by the establishment in 1984 of the Club Med-terrace resort on the until then neglected Providenciales, the westernmost inhabited island of the TCI chain and now the focus of numerous up-market tourist hotels as well as condominiums and villas.

Islanders and expatriates alike accord credit not so much to the French company itself, which has a penchant for pioneering undiscovered locations and was plied with elaborate concessions.

Rather, it required what is now seen as a leap of faith among British officials who committed funds on a previously unheard-of scale to accommodate what would be previously unseen numbers of visitor arrivals.

The funding, used for infrastructural needs such as upgrading the airstrip and roads, led at one stage to strident questioning by British parliamentarians in the House of Commons Public Accounts Committee.

The decision was vindicated. Club Med was followed by a stream of other developments. The direct inflow into government coffers from tourist levies, from a barely significant \$60,000 at the beginning of the decade, by two years ago was running at 10 times that

level and is forecast to reach \$1.7m this year.

By this measure the income from company registrations is in fact larger, at a projected \$2.2m for 1989-90. But the contribution the labour-intensive tourist business makes to the wider economy is far more thoroughgoing.

Stricter controls on public sector purse strings have also helped. The 1986 commission of inquiry into alleged corruption and other malpractices under the then Progressive National Party government found that "the Public Works Department wages bill has in the past been grossly inflated" by taking on more people than were needed, in a type of unofficial social welfare mixed with political patronage.

When elected government was restored in March 1988, not all their previous powers reverted to ministers. Crucially, the Governor and his officials now have direct responsibility for public ser-

vice appointments.

The increase in development activity on the islands has meant that the government wage bill is set to top \$10m for the first time this year, having roughly trebled over the decade. But proportionately less of locally generated revenues (ignoring the UK contribution) is immediately going out again to its own employees. At the start of the 1980s public sector-pay was absorbing more than three quarters of what the islands were earning by that measure, and in 1986-87 was still taking two thirds. Last year it was down to barely half, and the forecasts for 1989-90 indicate that wages and salaries will require an only slightly higher 82.5 per cent of recurrent revenue.

A further contributor to the financial turnaround has been privatisation. The scale, as always in the TCI, has been limited, and one significant move came in 1986 when the authorities moved to shed their

loss-making utility interests.

In one instance Mr Bob Blanchard, a Florida businessman who already owned the power generators on Grand Turk, took over the transmission and sale of electricity on that island for a nominal \$1 payment. But the company has since invested \$1.25m in upgrading equipment, the annual saving to the government is put at around \$1m, and service is by common consent far better.

Trends in power consumption provide only a rough guide to economic development as a few of the very largest users have licences to generate their own private supply. Nevertheless, electricity use grew 13.4 per cent last year.

Cable and Wireless of the UK, which runs the territory's telephone system, showed a similar 16.3 per cent increase in metres of cable with the number of subscribers growing at an even faster rate of 25 per cent.

Government revenue and expenditure (US\$m)						
	1980/81	1985/86	1986/87	1987/88	1988/89	1989/90*
Total revenue	7.355	16.552	17.199	18.081	24.148	44.350
Recurrent - Tax	2.269	7.072	6.483	10.526	15.242	18.028
Import duty	1.851	4.124	4.566	5.874	7.222	8.000
Export duty	0.72	0.130	0.175	0.148	0.140	0.140
Company registrations	0.139	1.129	1.414	1.556	1.800	2.200
Communications tax		0.054	0.228	0.252	0.280	0.330
Stamp duty	0.289	0.830	1.157	1.294	1.800	1.820
Work permits	0.060	0.379	0.505	0.730	1.300	1.718
Tourist levies	0.050	0.426	0.439	0.685	0.700	0.820
Recurrent - Non-tax	2.514	2.942	2.413	2.505	4.403	4.288
Rents	1.049	0.934	0.267	0.222	0.320	0.402
Fees, sales	1.556	1.912	2.084	2.182	3.983	3.714
Fines & forfeitures	0.309	0.096	0.052	0.121	0.100	0.150
UK budgetary aid		0.044	0.033	0.137	0.130	0.143
UK technical co-operation	2.171	3.921	3.254	2.892	8.138	23.780
Other	0.044	0.070	0.017	0.013		
Total expenditure	9.151	18.539	18.758	17.824	23.691	43.990
Recurrent expenditure	6.881	12.981	13.266	14.702	17.315	20.032
Wages & salaries	3.915	6.289	7.266	7.466	8.849	10.652
Other services	2.570	4.729	4.293	5.842	6.914	7.644
Interest	0.123	0.453	0.445	0.486	0.362	0.374
Subsidies	0.235	1.319	0.802	0.392	0.367	0.699
Other transfers	0.048	0.211	0.461	0.516	0.502	0.692
CDB subscriptions etc	0.008	0.007	0.005	0.069	0.111	0.038
Total capital expenditure	2.252	3.551	3.488	3.083	6.266	23.923
Recurrent revenue						
Less Recurrent expenditure	-1.716	-0.401	0.642	0.282	0.457	0.227
Total capital receipts						
Less Expenditure	-0.037	0.484	-0.184	-0.011		

\* Estimated; 2. Caribbean Development Bank

**Road to better times**

Continued from Page 1

But claims that certain public officials "have recommitted themselves to these things on a much grander scale".

The Chief Minister has capitalised on the PNP's drug associations to take a hard line on the narcotics trade - calling for the death penalty to be imposed for traffickers. The British Government would be unlikely to countenance the granting of such a power, although the TCI does nominally retain hanging for certain forms of murder.

The islands' association with the drug business has a long history, but its present extent is more difficult to measure. Washington officials decline to single out the TCI as any more than one of several Caribbean locations which have been used as trans-shipment points. Surveillance has been stepped up, but use of the potent form of cocaine known as crack has recently become evident in Provo, indicating that supplies are still finding their way through.

Keeping out drug-generated cash is another concern, but one which those involved in the TCI financial sector say they have amply addressed through limits on deposit-taking.

They argue that they cannot afford any sort of scandal, involving drugs or otherwise, because new business would be lost.

Drugs surveillance has been stepped up, but use of the potent form of cocaine known as crack has recently become evident in Provo

will provide a sufficient safeguard against abuses. One leading sceptic is Mr Liam Maguire, a California-based entrepreneur and former TCI government minister. He describes some finance dealings in the islands as having had "a stench that reached Los Angeles" and adds: "Anybody who is talking about the financial future of this place should not talk about the introduction of capital, but about the introduction of ethics."

In the hot-house that is Grand Turk's business and political world, such sentiments are not popular. Dissent is discouraged, past lessons often seem ignored.

Although the integrity of most who work there is beyond doubt, the expatriate community and the TCI's own leaders may need to concoct a rare blend of unanimity, vigilance, and a greater degree of tolerance if these distant, flat smudges of earth are to gain international allure as anything more than a seven-day package suntrap.

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**TURKS and CAICOS 3**

**UK RELATIONS**

**Bond forged by necessity**

A DECADE which began with Britain planning big development aid projects, intended clearly as a going-away present, had its heated climax in 1986-87 with a stern reassertion of parental control, and will end with the Turks and Caicos, if anything, further from independence than 10 years ago — and quite happy about it too.

The islands gained their own constitution only in 1976 after periods of attachment variously to the Bahamas and Jamaica. From this history the only residual tie is one of legal redress through the Court of Appeal in Nassau.

For TCI "belongers", the bond to the UK is forged by necessity rather than emotion. Policy initiatives which emanate from Whitehall are sometimes seen locally as remote or misguided, but on the whole the relationship seems valued not just as a source of aid, but also as a cautious countervailing force against any excesses on the part of their leaders.

This, in turn, is born from the islands' short and, so far, sorry experience of elected government. A two-party system has developed in which the sides have almost indistinguishable views on policy but cannot be reconciled on a personality level. A change to multi-member constituencies, intended to provide a more even representation in the Legislative Council, instead resulted last year in a landslide victory for Mr Oswald Skipings' People's Democratic Movement, and Britain may

need in the future to consider other constitutional means towards greater political accommodation.

In a rare example of unanimity, there exists an unwritten moratorium among rival political leaders not to campaign for independence. The pact, reached during the suspension of elected rule ahead of last year's election, is said by all to be good for about 10 years.

In law-making by the TCI government, officially the UK approach is one of "non-disallowance" whereby legislation emanates from the will of Legco, as filtered through the Executive Council where Britain's interests are represented by ex officio appointees. In practice, however, Britain through the Governor retains wide-ranging direct powers relating to the peace and good order of the territory. Among other things, development projects of any size are also referred to London.

This last power largely reflects the prevalence of Crown land, which London is willing to see alienated only if it is developed in a way that can be said to benefit the com-

munity. Residential title is granted on a so-called conditional purchase lease, and deeds are transferred only when a dwelling has been built. A similar arrangement applies to commercial projects, although freeholds are by no means as readily available.

In each case there have been abuses, usually involving the procurement of islands to act as "front" for a foreign purchaser, but such transfers are being more closely monitored than in the past. But there remains, whichever of the two main parties forms the government of the day, a belief among islanders that its supporters will be the more favourably treated.

Given the directness of the UK relationship, TCI links within the region are patchy. Ministers participate in a regular government conference, and the territory is a member of several organisations including the Caribbean Development Bank — where it has recently regained a better credit standing after a poor repayment record inhibited the granting of new loans between 1981 and 1988.

In trade, there has been little need for a strong regional bonding as the islands are not export suppliers of goods or produce except seafood. The chief export of the Turks and Caicos, in fact, been labour, particularly to the Bahamas where young people have gone in their thousands to seek work. Unskilled labour is also imported, notably build-

ing labourers from Haiti on short-term contracts, plus a swathe of illegal migrants from there and the neighbouring Dominican Republic.

The TCI government is unhappy about this two-way flow, with the loss of its young adults on the one hand, and on the other the social tensions it believes the influx is causing. But in the absence of more consistent employment prospects for its own populace, ministers appear to have little remedy.

Further afield, the main day-to-day ties with the UK on a governmental plane are paralleled by the pervasive influence on the islands of the US. This occurs:

- On an economic level, as the dominant trading partner and through the islands' use of the US dollar, as well as in the significant receipts derived from US tourism, property purchases mainly on Providenciales, and offshore financial transactions.
- Culturally, through the American television networks which are received via satellite into most homes.
- In law enforcement, because of Washington's wish to oversee the islands' use of its perceived "back yard".
- In the 1960s to 1970s the US used Grand Turk as an armed forces base, but satellite tracking and other technological developments eventually led to the withdrawal of this presence. The main sphere of operations now is in the offensive against drugs.

Anglo-US agreements have spawned a spotter plane and patrol boat to detect supplies being dropped in the area from light aircraft.

As a deterrent to drug-related funds, TCI financial institutions have agreed a code of practice which limits cash deposits to \$5,000, half the level which is permitted in the US before federal alarm bells ring.

OFFSHORE FINANCE business is intended to provide the second of the twin tracks to economic growth for the Turks and Caicos, with the authorities and local private sector professionals hoping that the passage of new banking, insurance and trust legislation will accord the islands' financial sector the same cachet that the TCI tourist industry already enjoys — as an exotic location, undoubtedly, but one which is secure.

After some delay, the new legal package is expected to be complete by the end of the year. To a large extent it will update and codify existing practice in a sector which has grown from nowhere during the 1980s and, for all its lack of regulation, has remained strikingly free of public scandal.

A handful of small banks has collapsed over the past several years, causing some local distress, but their international involvements were minimal. The sector's main, and painfully felt, setback was external — the implication of senior ministers in drugs and malpractice during the middle part of the decade resulted in unsurprising, but none the less, a loss of public confidence in which the business is only now recovering.

Financial practitioners in the capital Grand Turk, while insisting that there was no marked outflow of client funds, do admit to a certain uneasiness that the episode did bring new business screaming to a halt.

Existing banking laws had in any event inhibited the large-scale arrival of fringe or brass-plate institutions. There are only five groups sanctioned to perform any form of mainstream banking activity.

However, the islands have developed a thriving line in related areas, primarily company formation, trust business, and certain specialist forms of insurance. Central controls here have until now been all but non-existent. One choice which thus arises is whether the TCI graduates to become a full-line offshore centre or concentrate on specialist services of proven success. A related question is whether the new laws and their accompanying regulations — still unseen in their final form — might yet stifle the infant.

Mr Derek Sambrook, the newly installed supervisor of the offshore finance unit, has spent the last 10 years as a practitioner in that industry, most recently with a private trust company in the Isle of Man. He confesses to being the archetypal "poacher turned

**BANKING AND FINANCE**

**Thriving haven for companies**

gamekeeper" before anyone else can pin the label on him, but goes on to issue a more pointed warning about the background he brings to his job. "While any private sector delights in saying, 'Fine, we have a supervisor we can relate to', they must also realise they have someone who knows all the tricks — or at least a considerable number of them."

He is charged with the dual, some would say invidious, role of regulating the offshore centre internally and at the same time promoting it abroad. He and others in the administration speak earnestly of the need neither to over-nor to under-regulate an industry which will have a hard enough time convincing potential investors that the TCI offers a safe but responsive haven in which to spread risk, without becoming the next natural home for other people's rejects.

Financial practitioners argue that the small size of the community itself limits wrongdoing. "It is relatively easy for someone to get a bad reputation down here," says Mr Joe Connolly of Coopers and Lybrand, the only big accounting firm with a direct presence on the islands. "The grapevine works, and things are reported to government."

But Mr Sambrook, while expressing a favourable opinion of the financial professionals he has met during his first three months in the job, acknowledges readily: "Our credibility is eggshell thickness."

Adding that his unit is already forging links with British and US regulators to check the past and present standing of companies and individuals, he is determined that in the first year especially we have to tread lightly. We can't afford to make mistakes."

Scrutiny of the TCI plans has also become rather more intense since the financial sector in Montserrat, another British dependency in the region and of roughly equal size and sophistication, was this year blinded by a Roman Candle of exploding fringe institutions. The Montserrat collapses have seriously set back that territory's aspirations as a Caribbean

banking centre, arguably providing the TCI with a vacuum to fill just as the British Virgin Islands picked up considerable business from 1985 onward which might have gone to the Turks and Caicos had its political reputation been better.

Those seeking a banking or insurance licence will need to submit:

- A business plan indicating their intended areas of operation;
- An explanation why a base is being sought in the TCI;
- Balance sheet details with two years' forward projections; and
- Directors and shareholders to a vetting procedure.

Even before the new ordinances are in place, large institutions are coming forward. Toronto Dominion Bank, the Canadian banking group, was earlier this year granted a licence, joining its long-established compatriot, Bank of Nova Scotia, which shares the islands' retail banking business with Barclays of the UK.

The locally-managed Turks and Caicos Banking Company, controlled through a Liberian company, and the Providenciales-based West Atlantic Bank and Trust also operate in the territory but their clientele is hand-picked. According to Mr Anton Faessler, the Swiss-born managing director of Turks and Caicos Banking, "We don't accept cash deposits. I don't accept anybody I don't know with a suitcase of money."

No US banks are yet represented on the islands, despite the American dominance of tourist traffic, nor does Toronto Dominion intend to set up a high street presence. Officials at the bank's Canadian headquarters say the new entity will be a deposit-gathering operation for large-scale commercial funds, similar to an existing unit it has in the Cayman Islands.

In addition, one respected but still unnamed private foreign banking group has, out of a number of inquiries, come forward with an offshore licence application which the authorities say meets their preliminary requirements. These are likely to begin boosting the aggregate deposit base for

Turks and Caicos banking institutions which, after a 23 per cent leap in 1987, showed slower growth last year, rising 8 per cent to \$72m.

Outside banking, the TCI have developed a thriving line in corporate formations, with the emphasis on speed of service. A new company can be registered within a day, compared with up to a week in some other offshore jurisdictions where proposed names have to be cleared laboriously. Of the 1,444 registered last year, nearly all — 1,174 — were classified as exempt or foreign categories which also now make up nearly three quarters of the total 6,729 companies with a TCI registration.

This should remain a growth area even if the islands have come too late to mount an across-the-board challenge to full-service offshore locations.

If niche activities outside banking proper are to be the TCI's way forward, one local firm has staked out what it claims to be a world number one position, which would be the territory's first such title in any financial segment. Mr Reg Bodhanya, managing director of Morris Cottingham, an accountancy-based practice which through other offshoots is also active in corporate and asset management, says that his group represents some 700 credit life insurance companies in the US out of about 800 registered — TCI, a figure which last year surpassed the number incorporated in Arizona, the previous favourite domicile.

These are short-term life policies which car dealers typically require their private, hire-purchase customers to take out for the period of the loan. The risk is undertaken by a US insurance major but laid off partially through reinsuring in a tax-efficient jurisdiction elsewhere. At this stage the vehicle dealership, having collected a small and regulated commission as agent for the original policy, can get back on the act. Larger dealers have been frequently emerging as part-owners of the reinsuring companies — which may sound like bringing the liability back home to roost but instead usually offers a further profit slice to the motor showroom. Mr Bodhanya believes as much as half the entire US car market is now covered in this way.

This very specialised sector makes up the bulk of the insurance company registrations in the TCI, and most of the few dozen others are expected to depart rather than face regulation.

- 1 Detailed cost plans and estimates of overall project budget
- 2 Realistic timetables including full detailed information on different tender systems, absorption/capture rates, market profiles and accurate inventory counts
- 3 Cash flow, Applications for Finance presented in the form required by lending institutions
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**TURKS AND CAICOS ISLANDS**  
Expansion of the Offshore Financial Centre: New Unit leads the way.

Since the enactment of the Companies Ordinance 1981, the islands have become increasingly popular among a diverse range of end-users including attorneys, tax advisers and private investment banking institutions. Significant refinements to the 1981 Ordinance have now been introduced by amending legislation to come into effect shortly.

The islands have gained popularity for the following reasons:

- They are politically stable being a British Crown Colony with a history of peace and a low crime rate.
- They are geographically well-positioned, in the same time-zone as New York City.
- The official currency is the U.S. dollar; there are no exchange controls.
- There is no direct taxation of any kind.
- Government fees are lower than in most competing jurisdictions and professional fees are competitive.
- The Companies Registry is extremely efficient. As a matter of course, a company is incorporated on the same day as the application is lodged, with incorporation documents usually being completed and available within twenty-four hours.
- A flexible companies law giving rise to highly streamlined procedures of statutory administration.

**OFFSHORE FINANCE CENTRE UNIT**  
The recent inauguration of the Offshore Finance Centre Unit, with its corps of specialist staff, marked a significant stride forward in the progressive development of the islands as an international centre of finance and investment. Head of the Unit is a former bank inspector, with ten years experience in offshore trust and corporate management, Derek R. Sambrook, who as Supervisor of the Unit will play a key role in extending the fields of banking, trusts, companies and insurance as well as vetting applications for banking and insurance licences. The Deputy Superintendent is Raymond H. Checkley, a lawyer of long experience in the islands, who will also remain Registrar of Companies as well as Registrar of Trade Marks and Patents and of Shipping.

**PROCEDURE ON REGISTRATION OF A COMPANY**  
There are two main types of companies, ordinary and exempt.

The procedure on applying to register both is basically the same. Three copies of the Memorandum and Articles of Association are lodged together with the prescribed fee. The Subscribers must file a declaration that the operations of the company will be carried on mainly outside the islands. Agents lodging an application must hold the appropriate licence under the Business Licensing Ordinance—see below.

All companies must have a registered office within the islands and exempt companies must nominate a representative resident in the islands for service of process.

- Special privileges attaching to exempted companies.
- Confidentiality: No requirement to file details of shareholders or directors.
- Authorized capital may be expressed in any currency with no minimum paid-up capital requirement.
- Company name can be in any language, with no requirement for the word "Limited" to form part of the name.
- Objects may be unrestricted.
- No requirement for annual general meetings of Shareholders.
- Availability of Governor's Undertaking concerning exoneration from future direct taxation and any increases in annual filing fees for up to twenty years.

**TRANSFER TO AND FROM OTHER JURISDICTIONS**  
Part IX of the Companies Ordinance makes provision for the transfer into the islands of companies incorporated in other jurisdictions. The Law of the country of incorporation must not prohibit such transfers and there are safeguards to protect creditors and shareholders.

A company wishing to transfer in the future may obtain a "standby" permit which can be activated at short notice.

**GOVERNMENT FEES FOR COMPANIES**  
Fees are unlikely to be increased in the immediate future. Currently, the fee to register an ordinary company with a nominal capital of up to \$50,000 is \$275. The fee to register an exempted company with a nominal capital not exceeding \$5,000 is \$225.

The annual fee is \$250 for ordinary companies and \$300 for exempted companies.

**BANKING**  
A revised banking law has been approved by the Legislative Council and, together with regulations designed to control bank licensing and to regulate licences, will come into force shortly. The Superintendent is responsible for the issue of banking licences and will deal with all licensing applications. Regulations govern procedures and prescribe the fees. There are two types of licence: a National Banking Licence (NBL) and an Overseas Banking Licence (OBL). The NBL entitles the licensee to carry on banking business in and from within the islands with islanders and other residents of the islands.

The OBL entitles the licensee to carry on the same business from within the islands except that it may not accept deposits from, or lend to, any resident.

- A bank may hold both types of licence, provided that accounting is kept separate or the operations are through separate branches.
- There are no fixed minimum capital requirements. A more flexible system leaves more discretion to the Superintendent.
- All banks must file a business plan.
- Banks are not required to retain a prescribed reserve fund. NBLs, however, must maintain sufficient assets in the islands to meet all liabilities as they fall due.
- A holder of an NBL must file monthly and quarterly statements. A holder of an OBL has to file less detailed returns on a quarterly basis.

**INSURANCE**  
An entirely new Insurance Law has been approved by the Legislative Council and, with regulations to control the licensing and, with monitoring of insurance companies, should come into force shortly. Supervision will be in the hands of the Superintendent.

- No insurance business may be carried on in or from within the islands without the appropriate licence, being one of the following: an Insurer's Licence, an Insurance Agent's Licence, and Insurance Broker's Licence, an Insurance Manager's Licence, a Principal Insurance Representative's Licence or an Insurance Sub-agent's Licence.
- Every insurer will be required to submit a business plan.
- Auditing, annual accounts and certificates of compliance will generally be required, although the extent of monitoring will depend on the nature of the business.
- Insurer's representatives, whether brokers, agents or managers, will also have to lodge a business plan with an annual declaration of compliance.
- Every licensed insurer must file annual returns within three months of the end of its financial year. Information filed will include, where appropriate, asset confirmations, financial statements, actuarial valuations and guarantees. The Governor may relax these requirements in appropriate cases.
- Regulations will prescribe a fee structure which it is believed will be highly competitive.

**TRUSTS**  
A draft law on trusts has been presented to the Legislative Council and is expected to be enacted in the next few months. It is modelled on Jersey Law and when in force should prove a powerful attraction for businessmen and investors seeking a secure jurisdiction for their assets or those of clients.

**CONFIDENTIALITY**  
There is a general statutory duty of confidentiality upon banks, professional advisers, Government Officers (including the Unit) and other holders positions of trust. There are criminal sanctions for unauthorized disclosures. The islands do not party to any Double Taxation Agreement.

For further information contact:  
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Turks & Caicos Islands  
B.W.I.

TURKS and CAICOS 4

TOURISM

Tranquil and friendly destination

THE SWANEES (flamingoes) might be less in evidence now than when the early British explorers came to the islands en route to America...



Turtle Cove Marina, Providenciales: the island is a retreat for the worldly-wise

The friendly disposition of TCI "belongers" is one of the territory's best selling points. It is being marketed as a tranquil, top-drawer destination...

The sixth of July we came to the island Caycos, wherein Fernando said were salt ponds, assuring us if they were dried, we might find salt to shift with, until next supply...

American sphere of operations - and, it is said, the most profitable, turning over \$1m a week in its winter high season...

If Providenciales did not exist, the world tourism industry would arguably have found it necessary to invent it. Indeed, in many ways it has. The island has become a retreat for the worldly-wise...

those in the soaring local property sector who were becoming worried that Whitehall might have regarded such infusions as an historical one-off of the early 1980s...

the government's document on tourism policy, approved last year, says it "recognises that tourism is a fragile and sensitive industry, influenced by economic recessions in source countries..."

During the cheeper summer months the resort attracts a substantial proportion of holidaymakers from Europe. Many of them are also attracted by the club's dive operation...

British development aid to the tune of \$5m is this year being used to resurface the island's airport runway...

The issue is important because the islands aim to nurture a large number of permanent home-owners in Provo, even if they are not permanent dwellers there...

Nevertheless, five years since it opened, Club Med Turkoise has established itself as one of the most popular villages in the French company's

the February peak rate costs \$1,350 per person for double occupancy, some \$150 more than Guadeloupe, the next dearest, nearly a third higher than the average...

Not is price competition expected to develop to any great extent within the TCI. A spate of new hotel developments under way will emerge at the premium end of the market...

These are nothing compared with the funding problems which have bedevilled Provo's proposed Sheraton development, a 229-room hotel where work has been halted for the best part of two years...

A 200-room establishment to be managed by the US Radisson chain was by this month more advanced in planning than a rather larger development of more than 400 rooms put forward by a Nevada-based consortium...

THE MAN from Pan Am put it bluntly, as he curled his fingers inward. "We've got you like that," the assembled travel trade was told at the islands' first solo British promotion in London last month...

Although an increasing number of charter flights from North America provide weekly replenishment for the resorts of Providenciales, most TCI visitors enter via the Pan Am monopoly scheduled route from Miami...

There is no scheduled passenger shipping services and only an occasional cruise ship has called

ing a more leisurely approach can find connecting flights from some nearby Caribbean islands through regional carriers such as Bahamasair and the islands' own Turks and Caicos National Airline (TCNA)...

Sea cargo services are operated from Miami, but much of the freight, like all of the passenger traffic, comes by air. Rival airlines transfer their

COMMUNICATIONS

Flying monopoly

passengers to Pan Am for the final hop. Virgin Holidays, part of Mr Richard Branson's UK leisure empire, has been selling packages to the TCI for the past two years...

Will the position change? Local tourism authorities are painfully aware of the problems that would occur if Pan Am's personal financial plight forced it into retrenchments on its Caribbean routes...

However, the government has been talking recently to at least one further US major, understood to be American Airlines, about introducing a parallel service perhaps from the north-east seaboard...

Longer-haul routes are hampered by the limitations of TCI airport runways, which are not designed to take airlines much larger than the Boeing 737s used by Pan Am...

Once on the islands there are two airlines. One is TCNA's fleet of mainly seven-seater planes, which all but the pro-

rest islanders use as a bus service. Maximum fare within the TCI is \$22 for the half-hour trip between Grand Turk and Provo. The other is Cable and Wireless, the British company, which operates a telephone system which is modern and efficient, although ferociously expensive for international calls...

The high cost, as with most things on the TCI, is explained by small volume. Calls to the UK cost \$3.30 a minute at peak rate, rather more than double the charge that applies in the other direction, while businessmen note that, unlike its sister company Mercury in the US, Cable and Wireless (West Indies) offers no bulk user discounts in the Turks and Caicos. There is just not much bulk," says Mr Martyn Robinson, TCI marketing manager...

The high cost of international calls from the islands is explained by small volume

The group's 20-year franchise has only about two years to run, and negotiations for a renewal are under way, with Cable and Wireless confident that it will be kept on - it has recently been adding new digital exchanges, for example. Asked if a rival with existing regional operations such as AT&T of the US could step in, Mr Robinson says: "It's a big world - anybody could come in and negotiate with the government. But in the real world, we are here, and we have a lot of kit in here."

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**TURKS and CAICOS 5**

**INDUSTRY AND FISHERIES**

**Future expectations are all at sea**

CASSAVA, cotton, sisal, salt, and seafood - all have had their time in the Turks and Caicos. But the time for all, as a means of support for any large amount of the working population, has gone. Prospects are slim that any future product will take their place.

Conversations about industrial or resource-based activity on the islands immediately veer in one of two opposing directions. Whether government minister, appointed official, or an operator within the private sector, there is either a resigned shrug to the inevitability of an externally fuelled economy through tourism and offshore finance, or an excitable exposition of the latest in a long line of feasibility studies which in the end have produced nothing but paper and consumed little except administrative time.

Cassava cultivation died out with the Arawak Indians in the 16th century, and the other two cash crops historically cultivated in the somewhat more arable west of the chain, bore testimony largely to the initial enthusiasm of the Loyalist settlers who arrived from the American South after the revolution.

The salt industry, established around the middle of the 17th century and based on the arid easterly settlements of Grand Turk, Salt Cay and South Caicos, lasted a good 300 years and was clearly what those islands could do best. Unsurprisingly, then, there are perennial hopes that it may be revived - the collapse of the business in 1964 came about because competing countries such as the Bahamas had made technological improvements which the TCI had not matched.

Just behind the double row of buildings which makes up Cockburn Town, the islands' capital on Grand Turk, lie its inland salinas or salt beds, now ragged, stagnant and unappealing. Last year the rights to a number of these and further salinas on Salt Cay were taken up by Sun Crystals, a US group, raising local hopes. But another season has come and local workers could again be employed in the industry. Mr Derek Taylor, the Minister for Commerce and Development under whose department the private sector office falls, says his understanding is that suit-

able financing has not yet been arranged.

Mr Taylor sees the main problem besetting the islands not as a lack of resources, skills, initiative, or even project funding, but transport. He wants to see an inter-island ferry service so that goods can

**Marine products remain the only significant export industry of the islands**

be shipped out from a central point, possibly by establishing port on the uninhabited West Caicos, the only island not to be bound by a coral reef.

The minister, a former senior customs officer, goes further, arguing: "We are strategically located in every respect you can think north/

south and east/west. We could have a trans-shipment point with European goods and goods from Canada coming here during their winter season for stockpile while their ports are frozen." West Caicos, he adds, could also be ideal for oil bunkering and would allow direct shipments of a variety of products from the UK in order to break the Miami stranglehold.

Meanwhile, marine products remain the TCI's only significant export industry, producing more than \$4m in annual revenues, mainly from conch meat but with lobster as an important, and premium priced, secondary catch.

In the face of this, though, comes one of the region's sadder conch-to-Newcastle stories: while South Caicos islanders are packing shellfish to be shipped abroad, hoteliers in Grand Turk balefully admit to serving lobster tails from frozen from Florida.

Mr Taylor, his point about transport problems thereby illustrated, says the government is at the same time concerned about overfishing and the illegal use of chlorox, a bleach dropped in the water to agitate shellfish and move them towards waiting boats.

The government is considering a closure of the lobster season for two to three years, while encouraging the extraction of scudfish such as red snapper which have been so far neglected. Mr Taylor says that Japanese boats hover just outside TCI waters "and we would love to know what they are catching".

A shift to scudfish would, however, mean venturing into deeper waters with bigger boats than the 16-footers which are now used at the traditional fishing centre of South Caicos and also to a large extent at Providenciales, where the business has become more recently established.

The half-dozen seafood packing companies which the islands support are nearly all US-controlled, but the local fishermen own their own craft and simply sell them their produce day by day. With the average lobster catch down to perhaps a third or a quarter of levels five years ago, managers of the plants say the capital needed to upgrade to larger ocean-going boats is just not available.

Mr Aiden Durham, leader of the Opposition and a representative of South Caicos on the Legislative Council, endorses the need to move into scudfish, which account for little more than a tenth of current fisheries exports. Fishing sustained his island even when the salt business disappeared, but he is concerned about the recent drift of men and boats to Providenciales, which he argues provides no better a livelihood.

"If we have a bad few weeks

here, it shows in the local economy," he says. "People can't pay their bills in the shops. We have had an exodus to Provo, but it's not good for us, and not good for the people who go. They have to boil two pots, as the islanders say - they have a wife and children for whom they have to provide, then they have to rent an apartment in Provo. Some have drifted back."

The haemorrhaging of young talent and initiative has been felt even more keenly when TCI "belongers" have gone abroad to seek the advancement which has not been available to them locally. This includes not only the academically-gifted - the TCI can offer no tertiary education and most of those who go overseas to seek it do not return - but also a range of other islanders who are most commonly to be found working in hotels or on construction projects in the Bahamas to the north.

Estimates of their numbers vary widely, with some clarity expected from a Turks and Caicos census due to be undertaken next year, the first since 1980. But it is believed that at least as many islanders are living abroad as those who have stayed.

**There is no tertiary education and most of those who go overseas to seek it do not return**

Mr Oswald Skippings, the Chief Minister, puts the figure as high as 40,000, but this would include second and third-generation families who, while retaining the right to abode in the TCI, have few real ties.

Mr Skippings hopes some will return as the pace of tour-

ist sector development steps up. He is optimistic about two large hotel projects proposed for Grand Turk but acknowledges that the capital would have difficulty in accommodating anything more than itinerant workers.

Nationals from Haiti to the Philippines have been brought into Providenciales to work on developments there while building workers particularly from North Caicos, which traditionally supplied a lot of labour for that industry, have headed abroad.

North Caicos may experience a return influx with the planned commencement of work on Parrot Cay, a small neighbouring island where Bovis of the UK is due to build a 50-suite luxury hotel and villas in a long-delayed \$200m project initiated by Mr Patrick Ellis. He has long-standing links with the TCI and hopes to employ as many as 200 islanders in the building stage.

An even larger \$635m proposal to develop the island by Mr Liam Maguire, a California-based British entrepreneur, could if successful provide an enduring activity for the islands including North and South Caicos in the neglected middle of the TCI chain between Grand Turk and Provo.

He has received outline endorsement from Mr Skippings for the elaborate plan, which would be the island's biggest development scheme. It involves dredging a deep harbour (between south and East Caicos rather than at the distant West Caicos as envisaged by Mr Taylor). From this, a "theme port" would be created to attract cruise ships. Funding for work in progress would be sustained by the sale abroad of aragonite, an ultra-fine sea-sand which the port dredging would yield. Aragonite is used in various manufacturing processes such as paint and also has applications in coal-fired power stations for limiting the exhaust gas emissions which cause acid rain.

Financing is, however, far from being fully in place, and will depend partly on the international response to a planned bond issue. This would be made a private offering in \$250,000 denominations convertible ultimately into land and offering residence rights - thought to be a way of attracting Hong Kong funds. Resources experts believe the project will also need not to depend too heavily on aragonite, as some sources of supply closer to US mainland consumers have been mothballed in recent years.

**Mollusc class of '89 prepares to graduate**

**Conch farm enterprise**

ELABORATELY encased as they slowly patrol the seabed off the eastern coast of Providenciales, some hundreds of thousands of conches this year carry more than the usual heavy burden of their pearly shells.

The mollusc class of 1989 is intended to form the first full commercial output from Calicos Conch Farm, and mark the graduation into reality of a 15-year dream harboured by Mr Chuck Hesse, an American biologist and engineer who runs it with a staff of 35 on behalf of Trade Wind Industries, the owner.

TWI, with about \$3.5m in capital, is owned by 15 North American investors. Mr Hesse describes it as "one of the few non-suitcase shareholder companies in this country", adding that there is no soft aid money in the venture, nor do the investors use it as an offshore financial manoeuvre. He expects it to be in profit in two years.

Turks and Caicos belongs have used conch as a sub-

stitute food for centuries, as has been the case in Cuba, the Bahamas and Belize - stocks elsewhere in the Caribbean have largely been depleted. Because of the Hispanic population it is also eaten in south Florida and has more recently become prized as a delicacy.

When Mr Hesse arrived on the islands in 1974 it was being sent dried to Haiti as bait for the fresh vegetable produce which the TCI lacked. He steered the fishermen of South Caicos in the direction of the Miami market instead, where they still sell most of their export catch, now in frozen form. The business ships between 600 and 700 tonnes a year abroad and is worth more than \$2m annually in export revenues.

Various schemes for conch mariculture have been proposed over the years as a way of strengthening Caribbean economies, but no one has stayed the course as long as Mr Hesse. He says of the countries in the region: "Their ability to be economically success-

ful is dependent on their natural resources" - and the TCI has fewer than most. He describes the conch as "an underwater cow or sheep", which eats only algae and needs no elaborate feedstock.

The main problem is keeping track of them in their early months. Mr Hesse has developed a hatchery where they are reared until they are about 3½ three and a half months old and 25mm in length. Although three quarters of the larvae will have been lost by then, survival rates are far higher than in the sea where they succumb to lobster and other predators. They are then put into a 100-hectare fenced ocean "pasture", leased from the government, where they spend the remainder of the year.

Calicos Conch Farm expects to produce 300,000 animals in the current year, rising to an eventual target of 1m. This would boost the islands' export capacity by as much as 20 per cent.

But Mr Hesse is not content



Calicos Conch Farm: the world's largest commercial conch-rearing operation

to stop there. He is looking to Hong Kong jewellery makers as a source of demand for the shell, the most striking thing about the animal, which on South Caicos is discarded from the fishing boat. He has experimented successfully with cultured pearls, as in oysters - they occur once every 10,000 in the wild in colours ranging from brown to a sought-after pink which can fetch hundreds of dollars apiece.

He is developing markets such as aquarium suppliers in the US - because of their feeding habits, juvenile conches are good for keeping fish tanks clean. Rather than retain his exclusivity, Mr Hesse also wants to sell franchise rights to start farms elsewhere in the Caribbean. For the meat itself he sees China and Japan, where conch is eaten, as important future markets.

He wants to add value to what is now a straightforward bulk product for the islands, by producing fillet portions which before packing are tenderised to break down the rubbery consistency which can thwart an inexperienced cook.

But he is resisting offers which he regards as side-tracking the enterprise. One group wanted to buy the whole business so it could supply the young as "conch escargots" to the New York restaurant trade. "I got into this business to grow meat," he says.

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Inquiries are invited from prospective mortgage lenders wishing to pursue the possibility of participating in our Providenciales developments. Full legal, accounting and banking references will be made available upon request to appropriately qualified parties.

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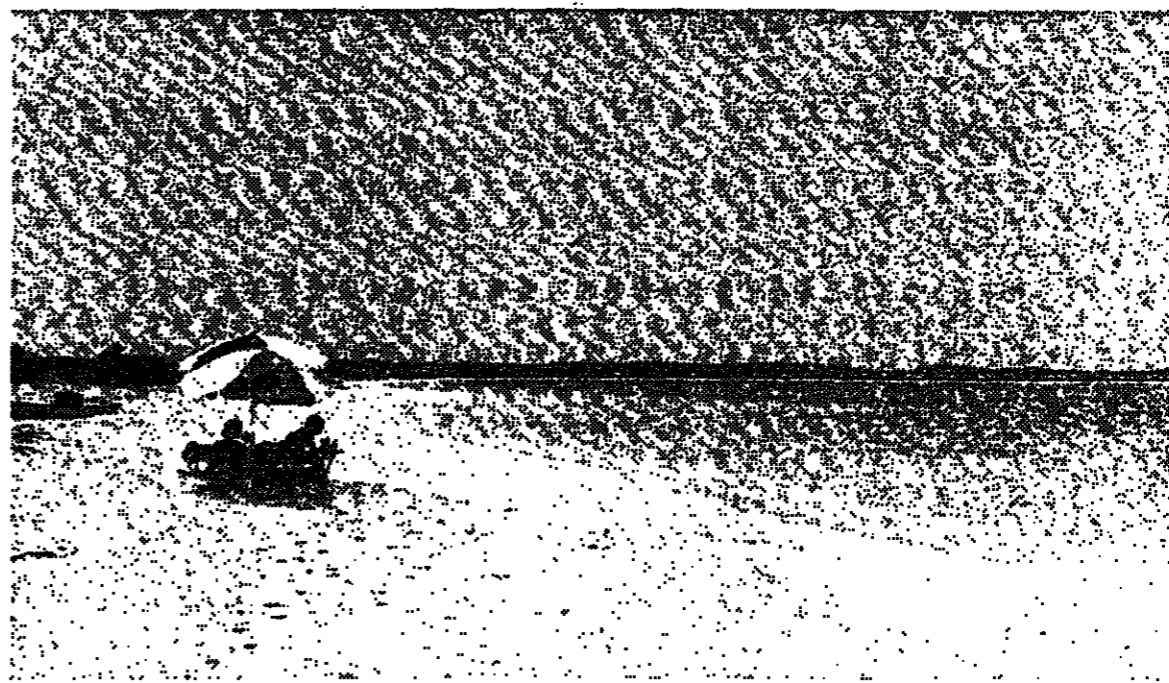
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FACSIMILE: (809-946) 4118



A crowded beach on the holiday island of Providenciales

**TURKS AND CAICOS, THE CARIBBEAN'S SECRET**

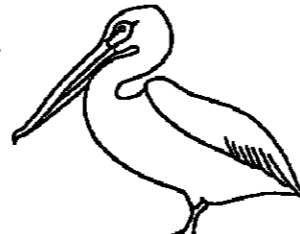
- COME - LAZE ON OUR 230 MILES OF GOLD AND WHITE SAND BEACHES
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**Turks & Caicos Islands**

FT UNIT TRUST INFORMATION SERVICE

For Current Unit Trust Prices on any telephone ring direct 0635 4 + five digit code (listed below). Calls charged at 38p per minute peak and 25p c/wk peak, inc VAT

AUTHORISED UNIT TRUSTS

Main table listing various unit trusts with columns for Unit Name, Unit Price, and other financial details. Includes sub-sections like 'Key Fund Managers Ltd' and 'Scottish Widows'.

GUIDE TO UNIT TRUST PRICING
These reports, the marketing, administrative and other costs which have to be paid by our members. These charges are included in the price when the customer buys the units.
The price at which units are sold is the price at which units are bought.
The price at which units are bought is the price at which units are sold.
The price at which units are sold is the price at which units are bought.
The price at which units are bought is the price at which units are sold.



FT UNIT TRUST INFORMATION SERVICE

For Current Unit Trust Prices on any telephone ring direct-0836 4 + five digit code (listed below). Calls charged at 36p per minute peak and 22p off peak, Inc VAT

Main table of unit trusts with columns for Name, Price, and other details. Includes sections for 'OTHER UK UNIT TRUSTS' and various insurance-related trusts.

INSURANCES

Table listing various insurance policies and their details, including AA Fraternity Society and others.

Continuation of the main unit trust table, listing numerous trusts and their current prices.

Continued on next page

FT UNIT TRUST INFORMATION SERVICE

For Current Unit Trust Prices on any telephone ring direct-0895 4 + five digit code (listed below). Calls charged at 38p per minute peak and 25p off peak, inc VAT

Main table containing unit trust information with columns for Fund Name, Type, and Price. Includes sub-sections for 'OFFSHORE AND OVERSEAS' and 'GUERNSEY (SIB RECOGNISED)'.

OFFSHORE AND OVERSEAS

GUERNSEY (SIB RECOGNISED)

MANAGEMENT SERVICES

LUXEMBOURG (SIB RECOGNISED)

JERSEY (SIB RECOGNISED)

FT UNIT TRUST INFORMATION SERVICE

Table of FT Unit Trust Information Service listing various unit trusts with columns for Name, Price, Yield, and other financial metrics.

LONDON SHARE SERVICE

Table of London Share Service listing various share funds and financial data, including sections for British Funds, British Funds - Contd, Loans, Foreign Bonds & Rails, and Money Market Bank Accounts.

LONDON SHARE SERVICE

AMERICANS - Cont'd

Table listing American stocks with columns for Stock, Price, Bid, Offer, and Dividend. Includes companies like American Express, American International Group, and American National Bank.

CANADIANS

Table listing Canadian stocks with columns for Stock, Price, Bid, Offer, and Dividend. Includes companies like Bank of Montreal, Canadian National Railway, and Imperial Oil.

BANKS, HP & LEASING

Table listing bank and leasing stocks with columns for Stock, Price, Bid, Offer, and Dividend. Includes companies like Citicorp, Citicorp Bank, and Citicorp Leasing.

HIRE PURCHASE, LEASING, etc.

Table listing hire purchase and leasing stocks with columns for Stock, Price, Bid, Offer, and Dividend.

BEERS, WINES & SPIRITS

Table listing beer, wine, and spirit stocks with columns for Stock, Price, Bid, Offer, and Dividend. Includes companies like Carlsberg, Heineken, and J & B.

BUILDING, TIMBER, ROADS

Table listing building, timber, and road stocks with columns for Stock, Price, Bid, Offer, and Dividend. Includes companies like Bovis Lend Lease, Bovis Lend Lease Construction, and Bovis Lend Lease Road.

BUILDING, TIMBER, ROADS - Cont'd

Table listing building, timber, and road stocks (continued) with columns for Stock, Price, Bid, Offer, and Dividend.

ELECTRICS

Table listing electrical stocks with columns for Stock, Price, Bid, Offer, and Dividend. Includes companies like British Electric, British Electric Services, and British Electric Supplies.

CHEMICALS, PLASTICS

Table listing chemical and plastic stocks with columns for Stock, Price, Bid, Offer, and Dividend. Includes companies like British Chemicals, British Plastics, and British Chemicals Services.

DRAPERY AND STORES

Table listing drapery and store stocks with columns for Stock, Price, Bid, Offer, and Dividend. Includes companies like British Drapery, British Stores, and British Drapery Services.

ENGINEERING

Table listing engineering stocks with columns for Stock, Price, Bid, Offer, and Dividend. Includes companies like British Engineering, British Engineering Services, and British Engineering Supplies.

ENGINEERING

Table listing engineering stocks (continued) with columns for Stock, Price, Bid, Offer, and Dividend.

DRAPERY AND STORES - Cont'd

Table listing drapery and store stocks (continued) with columns for Stock, Price, Bid, Offer, and Dividend.

ELECTRICS

Table listing electrical stocks (continued) with columns for Stock, Price, Bid, Offer, and Dividend.

CHEMICALS, PLASTICS

Table listing chemical and plastic stocks (continued) with columns for Stock, Price, Bid, Offer, and Dividend.

DRAPERY AND STORES

Table listing drapery and store stocks (continued) with columns for Stock, Price, Bid, Offer, and Dividend.

ENGINEERING

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ENGINEERING

Table listing engineering stocks (continued) with columns for Stock, Price, Bid, Offer, and Dividend.

ENGINEERING - Cont'd

Table listing engineering stocks (continued) with columns for Stock, Price, Bid, Offer, and Dividend.

ELECTRICS

Table listing electrical stocks (continued) with columns for Stock, Price, Bid, Offer, and Dividend.

CHEMICALS, PLASTICS

Table listing chemical and plastic stocks (continued) with columns for Stock, Price, Bid, Offer, and Dividend.

DRAPERY AND STORES

Table listing drapery and store stocks (continued) with columns for Stock, Price, Bid, Offer, and Dividend.

ENGINEERING

Table listing engineering stocks (continued) with columns for Stock, Price, Bid, Offer, and Dividend.

ENGINEERING

Table listing engineering stocks (continued) with columns for Stock, Price, Bid, Offer, and Dividend.

INDUSTRIALS (Misc.) - Cont'd

Table listing industrial stocks (continued) with columns for Stock, Price, Bid, Offer, and Dividend.

INDUSTRIALS (Misc.) - Cont'd

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Table listing industrial stocks (continued) with columns for Stock, Price, Bid, Offer, and Dividend.

INSURANCES

Table listing insurance stocks with columns for Stock, Price, Bid, Offer, and Dividend. Includes companies like British Insurance, British Insurance Services, and British Insurance Supplies.

LONDON SHARE SERVICE

For Latest Share Prices on any telephone ring direct-0836 43 + four digit code (listed below). Calls charged at 38p per minute peak and 25p off peak, inc VAT

LEISURE

Table of share prices for Leisure companies including Leisure Group, Leisure World, and Leisure Leisure.

PAPER, PRINTING, ADVERTISING - Contd

Table of share prices for Paper, Printing, Advertising companies including Newsprint, Printing, and Advertising.

TEXTILES - Contd

Table of share prices for Textiles companies including Textiles, Clothing, and Fashion.

TRUSTS, FINANCE, LAND - Contd

Table of share prices for Trusts, Finance, Land companies including Finance, Trusts, and Land.

OIL AND GAS - Contd

Table of share prices for Oil and Gas companies including Oil, Gas, and Energy.

MINES - Contd

Table of share prices for Mines companies including Mining, Metals, and Minerals.

MOTORS, AIRCRAFT TRADES

Table of share prices for Motors, Aircraft Trades companies including Motors, Aircraft, and Transport.

PROPERTY

Table of share prices for Property companies including Real Estate, Development, and Housing.

TRUSTS, FINANCE, LAND

Table of share prices for Trusts, Finance, Land companies including Finance, Trusts, and Land.

OVERSEAS TRADERS

Table of share prices for Overseas Traders companies including International, Global, and Foreign.

PLANTATIONS

Table of share prices for Plantations companies including Rubber, Palm Oil, and Forestry.

THIRD MARKET

Table of share prices for Third Market companies including Foreign, International, and Global.

COMMERCIAL VEHICLES

Table of share prices for Commercial Vehicles companies including Trucks, Buses, and Transport.

SHOES AND LEATHER

Table of share prices for Shoes and Leather companies including Footwear, Textiles, and Fashion.

TOBACCO

Table of share prices for Tobacco companies including Cigarettes, Tobacco, and Consumer Goods.

TRANSPORT

Table of share prices for Transport companies including Airlines, Shipping, and Logistics.

OVERSEAS TRADERS

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OVERSEAS TRADERS

Table of share prices for Overseas Traders companies including International, Global, and Foreign.

PLANTATIONS

Table of share prices for Plantations companies including Rubber, Palm Oil, and Forestry.

Miscellaneous

Table of miscellaneous share prices including various international and niche stocks.

THIRD MARKET

Table of share prices for Third Market companies including Foreign, International, and Global.

MINES

Table of share prices for Mines companies including Mining, Metals, and Minerals.

NOTES

Text providing information about stock exchange listings, company announcements, and market news.

REGIONAL & IRISH STOCKS

Table of share prices for Regional and Irish Stocks including UK, Irish, and European companies.

TRADITIONAL OPTIONS

Table of share prices for Traditional Options including various financial instruments and derivatives.

PROPERTY

Table of share prices for Property companies including Real Estate, Development, and Housing.

OILS

Table of share prices for Oils companies including Energy, Petrochemicals, and Refining.

MISCELLANEOUS

Table of miscellaneous share prices including various international and niche stocks.

CURRENCIES, MONEY AND CAPITAL MARKETS

POUND SPOT-FORWARD AGAINST THE POUND

Table with columns: Nov 24, Day's spread, Close, One month, % a.a., Three months, % a.a. Includes data for US, Canada, Netherlands, Belgium, Denmark, West Germany, Portugal, New Zealand, Italy, Norway, France, Sweden, Japan, Austria, Switzerland, ECU.

DOLLAR SPOT-FORWARD AGAINST THE DOLLAR

Table with columns: Nov 24, Day's spread, Close, One month, % a.a., Three months, % a.a. Includes data for UK, Ireland, Canada, Netherlands, Belgium, Denmark, West Germany, Portugal, New Zealand, Italy, Norway, France, Sweden, Japan, Austria, Switzerland, ECU.

FT-ACTUARIES WORLD INDICES

Jointly compiled by The Financial Times Limited, Goldman, Sachs & Co., and County NatWest/Wood Mackenzie in conjunction with the Institute of Actuaries and the Faculty of Actuaries

Table of FT-Actuaries World Indices for Friday November 24 1989 and Thursday November 23 1989. Columns include National and Regional Markets, US Dollar Index, Pounds Sterling Index, Local Currency Index, 1989 High, 1989 Low, Year ago (approx).

MONEY MARKETS Japan may follow the Fed's lead

THE BANK OF JAPAN seems unconcerned by the yen's fall against the D-Mark. It will certainly do no harm to Japanese exports and may be part of the reason why the Nikkei Index has hit record highs in Tokyo.

UK clearing bank base lending rate 15 per cent from October 5

This week the Bank of Japan is likely to inject liquidity into the domestic money market to prevent tight conditions leading to higher interest rates.

STERLING INDEX

Table showing Sterling Index values for Nov 24, 25, 26, 27. Columns include 8.30 am, 9.00 am, 9.30 am, 10.00 am, 10.30 am, 11.00 am, Noon, 1.30 pm, 2.00 pm, 2.30 pm, 3.00 pm.

EURO-CURRENCY INTEREST RATES

Table of Euro-currency interest rates for Nov 24. Columns include Start term, 7 days, One month, Three months, Six months, One year. Includes data for Sterling, US Dollar, Canadian Dollar, Swiss Franc, Japanese Yen, etc.

EXCHANGE CROSS RATES

Table of exchange cross rates for Nov 24. Columns include Nov 24, £, \$, DM, YFr, SFr, HFl, Lira, C\$, R\$. Includes data for DM, £, Yen, Franc, Mark, Lira, Dollar, etc.

FT LONDON INTERBANK FIXING

Table of FT London interbank fixing for Nov 24. Columns include 11.00 a.m., 3 months US dollars, 6 months US dollars, 90 days, 180 days, 360 days.

MONEY RATES

Table of money rates for Nov 24. Columns include Overnight, One month, Two months, Three months, Six months, Lending rate. Includes data for New York, London, etc.

LONDON MONEY RATES

Table of London money rates for Nov 24. Columns include Overnight, 7 days, One month, Three months, Six months, One year. Includes data for Interbank Offer, Interbank Bid, etc.

EUROPEAN OPTIONS EXCHANGE

Table of European options exchange for Nov 24. Columns include Series, Vol, Last, May 90, Aug 90, Dec 90, Jan 91, Feb 91, Mar 91, Apr 91, May 91, Jun 91, Jul 91, Aug 91, Sep 91, Oct 91, Nov 91, Dec 91, Jan 92, Feb 92, Mar 92, Apr 92, May 92, Jun 92, Jul 92, Aug 92, Sep 92, Oct 92, Nov 92, Dec 92, Jan 93, Feb 93, Mar 93, Apr 93, May 93, Jun 93, Jul 93, Aug 93, Sep 93, Oct 93, Nov 93, Dec 93, Jan 94, Feb 94, Mar 94, Apr 94, May 94, Jun 94, Jul 94, Aug 94, Sep 94, Oct 94, Nov 94, Dec 94, Jan 95, Feb 95, Mar 95, Apr 95, May 95, Jun 95, Jul 95, Aug 95, Sep 95, Oct 95, Nov 95, Dec 95, Jan 96, Feb 96, Mar 96, Apr 96, May 96, Jun 96, Jul 96, Aug 96, Sep 96, Oct 96, Nov 96, Dec 96, Jan 97, Feb 97, Mar 97, Apr 97, May 97, Jun 97, Jul 97, Aug 97, Sep 97, Oct 97, Nov 97, Dec 97, Jan 98, Feb 98, Mar 98, Apr 98, May 98, Jun 98, Jul 98, Aug 98, Sep 98, Oct 98, Nov 98, Dec 98, Jan 99, Feb 99, Mar 99, Apr 99, May 99, Jun 99, Jul 99, Aug 99, Sep 99, Oct 99, Nov 99, Dec 99, Jan 2000, Feb 2000, Mar 2000, Apr 2000, May 2000, Jun 2000, Jul 2000, Aug 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2033, Jan 2034, Feb 2034, Mar 2034, Apr 2034, May 2034, Jun 2034, Jul 2034, Aug 2034, Sep 2034, Oct 2034, Nov 2034, Dec 2034, Jan 2035, Feb 2035, Mar 2035, Apr 2035, May 2035, Jun 2035, Jul 2035, Aug 2035, Sep 2035, Oct 2035, Nov 2035, Dec 2035, Jan 2036, Feb 2036, Mar 2036, Apr 2036, May 2036, Jun 2036, Jul 2036, Aug 2036, Sep 2036, Oct 2036, Nov 2036, Dec 2036, Jan 2037, Feb 2037, Mar 2037, Apr 2037, May 2037, Jun 2037, Jul 2037, Aug 2037, Sep 2037, Oct 2037, Nov 2037, Dec 2037, Jan 2038, Feb 2038, Mar 2038, Apr 2038, May 2038, Jun 2038, Jul 2038, Aug 2038, Sep 2038, Oct 2038, Nov 2038, Dec 2038, Jan 2039, Feb 2039, Mar 2039, Apr 2039, May 2039, Jun 2039, Jul 2039, Aug 2039, Sep 2039, Oct 2039, Nov 2039, Dec 2039, Jan 2040, Feb 2040, Mar 2040, Apr 2040, May 2040, Jun 2040, Jul 2040, Aug 2040, Sep 2040, Oct 2040, Nov 2040, Dec 2040, Jan 2041, Feb 2041, Mar 2041, Apr 2041, May 2041, Jun 2041, Jul 2041, Aug 2041, Sep 2041, Oct 2041, Nov 2041, Dec 2041, Jan 2042, Feb 2042, Mar 2042, Apr 2042, May 2042, Jun 2042, Jul 2042, Aug 2042, Sep 2042, Oct 2042, Nov 2042, Dec 2042, Jan 2043, Feb 2043, Mar 2043, Apr 2043, May 2043, Jun 2043, Jul 2043, Aug 2043, Sep 2043, Oct 2043, Nov 2043, Dec 2043, Jan 2044, Feb 2044, Mar 2044, Apr 2044, May 2044, Jun 2044, Jul 2044, Aug 2044, Sep 2044, Oct 2044, Nov 2044, Dec 2044, Jan 2045, Feb 2045, Mar 2045, Apr 2045, May 2045, Jun 2045, Jul 2045, Aug 2045, Sep 2045, Oct 2045, Nov 2045, Dec 2045, Jan 2046, Feb 2046, Mar 2046, Apr 2046, May 2046, Jun 2046, Jul 2046, Aug 2046, Sep 2046, Oct 2046, Nov 2046, Dec 2046, Jan 2047, Feb 2047, Mar 2047, Apr 2047, May 2047, Jun 2047, Jul 2047, Aug 2047, Sep 2047, Oct 2047, Nov 2047, Dec 2047, Jan 2048, Feb 2048, Mar 2048, Apr 2048, May 2048, Jun 2048, Jul 2048, Aug 2048, Sep 2048, Oct 2048, Nov 2048, Dec 2048, Jan 2049, Feb 2049, Mar 2049, Apr 2049, May 2049, Jun 2049, Jul 2049, Aug 2049, Sep 2049, Oct 2049, Nov 2049, Dec 2049, Jan 2050, Feb 2050, Mar 2050, Apr 2050, May 2050, Jun 2050, Jul 2050, Aug 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## The Business Column

### Managing matrices in all but name

One of the main speakers at Brunel University seminar on matrix management last week was a senior executive from Harwell, one of the more commercially minded parts of the UK Atomic Energy Authority. His subject was the effectiveness of a widely admired matrix structure which Harwell has operated for 20 years, under which staff report in two directions at once: to a technical boss and to a business unit.

The timing of his presentation was, to say the least, paradoxical. For, as he revealed apologetically halfway through his remarks, Harwell's matrix is about to be abandoned. As part of a root-and-branch restructuring of the AEA into nine very market-orientated "businesses," Harwell itself is being dismantled. With it - theoretically - the whole matrix concept will disappear.

So how does the AEA intend to manage the many cross-business linkages technological and otherwise - which must continue to exist if there is to be any logic in the AEA's continued existence, other than political convenience?

Further signs at its headquarters of the admission that top management is currently wrestling with precisely this problem, and that it will probably end up with a number of matrix-like mechanisms albeit rather different from the Harwell model, and not necessarily called a matrix.

### Wariness

Given the complexity and bureaucracy which has bedevilled many matrix structures, in multinational companies at least as much as in the state sector, such wariness about the whole concept is understandable. In the appliances division of Electrolux, where a divisional/country matrix has had to be developed to cope with the Swedish company's rapid multinational expansion, some managers treat the word almost like leprosy.

The same shyness is applied increasingly to matrices of the type where functional disciplines such as technology, rather than just divisions and countries, form one of the dimensions. When BP Exploration (known internally as BPX) announced a dramatic delayering and restructuring programme in the early autumn, it studiously avoided using the word "matrix" to describe any part of its newly streamlined organisation.

Many of its technologists are indeed being transferred from the centre to BPX's various operating companies, in order to turn the latter into more complete business entities. Yet the BPX "technology centre" will retain what the company calls "functional parentage" of all technical staff.

What this means is not that BPX's matrix has been abandoned, but that the power balance within it has been shifted sharply away from central functions, and towards the operating companies.

### Demolition

This sort of balance-shifting is disruptive at the best of times. But it is infinitely preferable, in many circumstances, to the outright demolition of an organisation's structure which has served a company reasonably well, and which could continue to do so if only the people within it could learn to operate differently.

Changing the way existing structures are managed may be a lot less glamorous than a root-and-branch upheaval, but it can often be far more effective. Not, perhaps, in the case of impossibly complex and rigid matrices, like the one which Phillips abandoned a few years ago. Nor in many medium-sized companies, which actually need to add an extra dimension of co-ordination as they expand and "go global."

But many established large multinationals would do well to abandon their relentless search for "ideal" formal structures, and concentrate instead on creating a cohesive internal culture which allows the organisation to operate flexibly according to the particular requirements of time and place.

In the words of Christopher Bartlett and Sumatra Ghoshal, authors of *Managing Across Borders*, an illuminating new book on multinational management, the important thing is to "create a matrix in managers' minds."

## THE MONDAY INTERVIEW

# Dilemma of a Hong Kong superman

Li Ka-shing, chairman of Cheung Kong Holdings, talks to John Elliott

The man who represents Hong Kong's best known rags-to-riches story faces a dilemma. Some 30 years after starting a business empire now worth well over \$2bn (£1.9bn), Mr Li Ka-shing has divided interests and loyalties. These arise from the impact of Hong Kong's return to Chinese sovereignty in 1997 on his property-to-telecommunications group, headed by Cheung Kong and Hutchison Whampoa.

"If you are running a public company, it's not all your own personal money and you always need to consider what is best for the shareholders," says the 61-year-old, known to associates as K.S. Li. Shareholders and executive directors have urged him to follow other local companies and move his empire's domicile out of Hong Kong. "As of this moment I am not saying 'yes' to such a move. I don't like to see these sorts of things happening."

Mr Li knows that if he emphasises his empire's Hong Kong base, which accounts for 85-90 per cent of his public companies' assets, he will risk losing international investors who want a strong corporate strategy geared to 1997. So that percentage is coming down.

But any dramatic switch of domicile or investments would severely damage local and international business confidence because the companies, with capitalisation totalling HK\$72bn (£5.9bn), account for some 14 per cent of the local stock market. If Mr Li goes too heavily international, he will be accused of deserting the place which adopted him as a penniless immigrant from China in 1940. He would also suffer financially because, as one banker says, "Li is a belt-weather and if he is seen to be abandoning Hong Kong he will bring down the whole pack of cards here - and his own wealth - with him."

That poses a delicate balancing act for the colony's most astute speculator who is admired for knowing instinctively how to play the property and stock markets, when to

invest and, perhaps more important, when to give up and pull out fast. "In business you must be solid, quiet, have a budget, and anything over the budget you should give up right away," he explains. "Since 1950 there has not been a year when I have lost a penny on any business."

Mr Li is estimated to be worth some \$2bn when personal investments in property, hotels, banking and other sectors, started 20 years ago in

### PERSONAL FILE

1928: Born in Chiu Chow, southern China  
1940: Emigrated to Hong Kong  
1950: Founded Cheung Kong, making plastic flowers and toys  
1972: Took Cheung Kong public  
1978: Took over Hutchison Whampoa

Canada, the US and elsewhere, are added to his 35 per cent public stake in Cheung Kong.

A rather shy man, he runs his empire from a discreetly elegant 22nd-floor suite in a nondescript modern block called the China Building, located anonymously on one of the city's busiest street corners. That is in line with his life-style, which wins him the title "I enjoy a very simple life. My living standards are no different compared with 1950. I still live in the same house and I don't like black tie dinners," he says - though he acknowledges with obvious feeling that "people are jealous."

The jealousy stems from his grip on key sectors of the local economy including over 50 per cent of the container port, as well as an electricity utility, plus one of the largest local land banks and big property developments. His biggest coup came in 1979 when, as a self-made Chinese entrepreneur, he ousted the British owned Hutchison Whampoa trading company. That coup was sponsored by

the Hongkong and Shanghai Bank where he is now a deputy chairman.

Mr Li has no doubt that has made him successful so far and earned him his reputation for being a fair man to deal with. "The formula is so simple, but the work is hard," he says. "You do not spend much money on yourself, but you spend it on your friends. Be mean to yourself, but not to other people and build up a good reputation. Always keep your promise and automatically people will like to do business with you. If you are always fair with people - more than fair - business will come to you. More comes to me than I can handle."

Clearly there were big ambitions from the beginning, although Mr Li denies a colourful story that he started making plastic watch straps on a small rented balcony and slept at night under his machine. He insists his humble beginnings have been recounted too often, but then relaxes and talks enthusiastically about how he started making plastic flowers (he became one of the world's biggest producers) after he arrived in Hong Kong from Chiu Chow in the nearby Chinese province of Guangdong.

"At 14 I started working in the plastics industry and took care of my whole family. When I was 17 I was sending money back to my mother - more than she needed. Then I became a salesman, then general manager. In 1950, at 23, I started my own business."

But does a 14-year-old or a 22-year-old ever dream of \$2bn success? "I always had confidence when I started a small factory that sooner or later it would become much bigger. I built all this up step by step. When you are young you must work very hard. Others work eight hours, so you work 16. "Then you steadily get higher and higher, and because you keep your reputation people trust you and you get on well with people. Study at night and learn new things, learn a little bit more than your competitor and adopt new



'Be mean to yourself, but not to other people'

technology - I did that in the plastics industry. But the money will not come to you if you just relax and sleep; and of course you need some luck."

His advisers sometimes wish he would sleep more. He has a reputation for working all hours, through the night if necessary, when he is on a deal. That goes with his reputation for responding to offers within a day and of quickly getting out of projects that go wrong.

"I like friendly deals and I like people to come to me with business. That is my philosophy and I have told my two boys - never take advantage of anyone." He says his minority shareholders and tenants benefit from that. I don't like to damage a company. So many takeovers are unfriendly, creating damage in a good company and I don't like to see that. I buy a few per cent as a base to see if it is a good opportunity, then increase if it is. But if it is not good, I get out."

"The most famous targets which faced this approach include Pearson (which owns the FT) in 1986, Hong Kong Land (part of the Kewick family's Jardine empire) last year, and Cable and Wireless of the UK in which Mr Li owns a 4.9 per cent longer term stake because of his group's interest

in telecommunications. "I'll go anywhere in the world if there is a good rate of return, the country is stable, and there is proper legal protection."

He has tended to invest in assets, like property, which can be quickly traded. But he also has HK\$10bn tied up long-term in three terminals at Hong Kong's container port (out of a HK\$30bn-plus four-to-five year investment programme in the colony), and will bid for a fourth terminal next year.

He usually avoids labour-intensive companies. "Normally in western countries, if you get into manufacturing with a lot of employees, you will have to deal with unions and I don't like to have to face up to trouble with unions."

His straightforward approach to business has however been upset by the June events in mainland China. People who know him say he was shattered by the Peking hardliners' crackdown, but he refuses to say so openly. "Basically I am Chinese and China is my own country and I love my country. I am hoping that people will learn lessons and I hope they will never repeat things again. I was sad to see those television pictures on

June 4." Although he will not admit it, no one in Hong Kong has any doubt that these events added urgency to the group's decision to pull out of a local cable television bid that "went over budget" and, longer term, to reduce the proportion of its assets in the colony from the present 85 per cent-90 per cent to 70 per cent, or maybe even to 50 per cent. Mr Li resists discussing the figures and only says they "depend on the returns we find outside."

His takeover trail in Hong Kong however has almost certainly ended. "Our investment will continue in Hong Kong but not takeovers of companies. The chances of that are not high. Our percentage in Hong Kong is already too high."

He insists, with qualifications, that the "potential of Hong Kong is still there." He is only "reasonably" optimistic on the economy and he specifies "the coming 5-10 years" as the period when the colony will remain the group's "main money making place." About post-1997 he says: "You cannot forecast because you do not know whether you will have good returns or not because investment in south-east Asia is also very good today."

Mr Li is not willing to agree that Hong Kong is unique. Asked if he would rather start again there or somewhere else, he says: "Many other countries have good opportunities. It is not only Hong Kong - you can see in Taiwan, Singapore, Malaysia and Indonesia a lot of money because it is the basic thing of Chinese to work very hard."

Of future plans Mr Li says: "I hope before 1997 I can be retired, that is very possible." He has two sons - Victor and Richard - both in their 20s and both with Canadian nationality. That is where a lot of Mr Li's personal wealth is invested - including a controversial \$1.7bn housing, offices and services development on Vancouver's 204-acre Expo 1986 site approved last week.

He says he is not yet sure about his succession and seems to suggest professional managers might take over for a time. "The professional management teams are very happy and the sons still need time to learn. I don't know yet. But if you have a good team of management working together for so many years and you trust each other, it doesn't mean it has to be your sons."

## Private law and the public's right to know

Mr Justice Hoffman began his judgment last Wednesday in *Re Goodwin* in a typically bland, judicial manner: "This is a motion for an order requiring a journalist to disclose the contents of the information. The courts rarely make such orders because there is a well-established public interest in the confidentiality of journalists' sources." One might think that that was a prelude to the upholding of the journalist's duty to protect the confidential information he had received.

The case proved, however, to be one of those "rare" instances, because the judge held that the disclosure of the information was necessary "in the interests of justice." *Re Goodwin* strikes at the heart of press freedom and is thus destined to draw battle lines between Section 10 of the Contempt of Court Act, 1981 and Article 10 of the European Convention on Human Rights. Does the legal remedy for enforcing a private commercial interest have a higher social value than the protection of sources by journalists?

First, the facts. A privately owned company was engaged in a re-structuring of its financial affairs. It needed to raise additional working capital and was negotiating for a substantial bank loan. It employed well known accountants to prepare a corporate finance plan. Eight "strictly confidential" copies of a draft plan were distributed. The accountants' copy went missing and the next day Mr Goodwin, a trainee journalist on *The Engineer*, received information from an unidentified source. The circumstances pointed to the source having had access to the plan. Mr Goodwin retrieved some information about the company from newspaper cuttings and then checked his information with an employee of the company. That information clearly indicated some knowledge gleaned from the missing plan.



JUSTINIAN

Alarmed by the prospect of publication of its plan in embryo, before the new financing was in place, which might cause severe damage to confidence in the company among its customers and suppliers, the company hurried off to the High Court. The publishers were stopped for the time being from publishing. But the company feared other publicity might result from the source continuing his "whistle blowing" activities.

The public interest in non-disclosure of sources of information is subject to four heads of interest, of which "the interests of justice" is one. The law is that the court may not order disclosure unless it is satisfied that disclosure is necessary - not merely justified or expedient. These interests are said by the English courts, which were echoed by Mr Justice Hoffman, to be "superior" interests, or to "take priority" over the public interest in non-disclosure. It is this judicial interpretation of Section 10 of the 1981 Act that is open to debate.

Mr Justice Hoffman concluded that on the evidence there was a strong case for saying that the company had suffered a serious wrong. Furthermore, the company would suffer serious commercial damage from the publication of the information in the file during the immediate future. The judge accepted that the journalist's source might have received the information second hand.

The main thrust of the journalist's defence was that company could not reasonably expect to have the assistance of a journalist to investigate and deal with a leak in its security arrangements. This was not a case of national security. The judge rejected this argument. Legal proceedings must at least be contemplated for the interests of justice to arise, however. The availability of a legal remedy carries with it the citizen's right of unimpeded access to the courts. The expression "justice" is used in the technical sense of the administration of justice in the course of legal proceedings in a court of law. The company was entitled as part of its legal action to get disclosure of the source of the information.

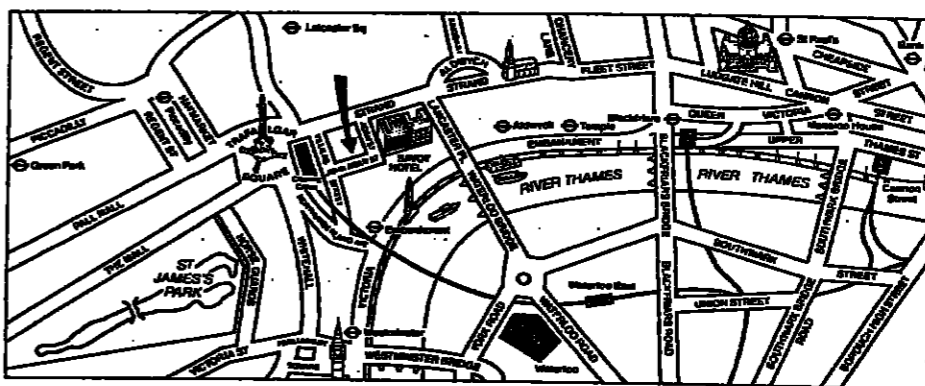
There is an essential flaw in the reasoning that leads to the conclusion that disclosure was necessary in the interests of justice. The reasoning tests the balance of interests - confidentiality in commercial activity and the journalist's duty to protect the sources of his information - in private law terms: citizen v citizen. However, the freedom of expression in Article 10 of the European Convention on Human Rights is constitutionally guaranteed and inures to the benefit of the public and not in the journalist in his own right. It is thus a public law right.

When the application was heard on Friday for Mr Goodwin's committal to prison for contempt in refusing to hand over the notes which could identify his source, the judge rejected the idea that the case involved a conflict between the company's private commercial interests and the public interest in the freedom of the press. "The conflict is between two public interests - the free availability of information and the fair administration of justice," he said. Not so. The first is the public's right; the second is only the public method by which an individual's private rights can be enforced.

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SECTION III

# FINANCIAL TIMES SURVEY



**Strikes, rising wages, a higher won and US trade pressure have brought a touch of cold reality to the**

**land of the economic miracle.**

**Stefan Wagstyl reports on South Korea's move towards a more democratic, more outward-looking and more market-oriented economy**

## Turmoil of transition

SOUTH Korea is struggling to come to terms with its own success.

After three years of unprecedented expansion, a sharp slowdown in exports has plunged Koreans into a deep bout of anxiety. Businessmen, who usually like to compare their country to Japan, instead talk darkly about Argentina, as an example of a once-rich country which squandered its resources.

The main concern is that over the past three years, rising wages and the appreciation of the won, have undermined Korea's export competitiveness. Strikes have sullied Korea's reputation as a land of industrial harmony.

But the truth is that the outlook is not as bad as some Koreans believe. The causes of the gloom are the deeply unsettling changes which Korea is undergoing as it moves from authoritarian to democratic government, from a state-led economic system to one in which market forces are to be given greater play. Foreign relations are at a sensitive stage as the country tries gingerly to establish contacts with North Korea.

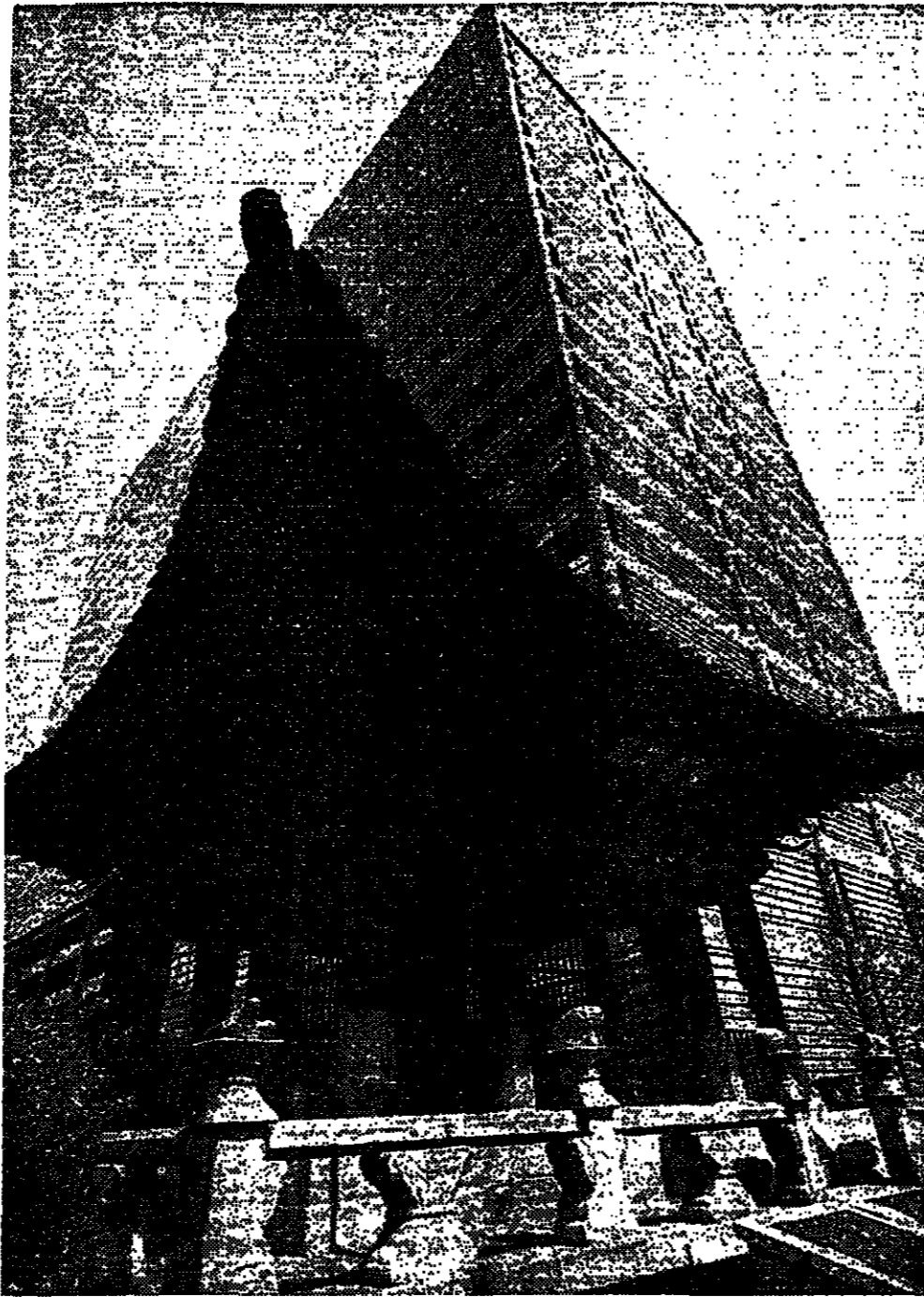
Also, Korea's trading partners, especially the US, are

insisting that the country can no longer enjoy access to export markets without dismantling the barriers which have shielded Korean industry for nearly 30 years of high-speed growth.

However, as well as bringing difficulties, these changes are creating opportunities for business: in investment at home and abroad, in access to international capital markets, in a home market of 45m increasingly rich people.

The International Monetary Fund in a recent report said: "The present difficulties should not be allowed to overshadow the impressive expansion, unequalled elsewhere in the world, that has been achieved by Korea's dynamic economy since 1985. As a result of its accomplishments the Korean economy is in a strong position to face the challenges that lie ahead."

The Korean conglomerates, or *chaebol*, led by Samsung with sales last year of \$31bn, Hyundai (\$25bn), Lucky-Goldstar (\$23bn) and Daewoo (\$15bn) should be best placed to take advantage, given their dominance. They are beginning to specialise more in key industries where they think they have an international



## South Korean Finance & Industry

competitive edge - notably Samsung in electronics.

The government also wants to encourage small and medium-sized companies to be more outward-looking. For foreign businesses too the upheavals could bring opportunities. Koreans are putting a special

emphasis on building contacts with Europe - to try to balance their relatively strong ties with the US and Japan. Korean bankers and businessmen are passing through Europe at the same time as President Roh Tae Woo, who is visiting Europe this week.

Traditional preferences for things Korean will not disappear overnight, any more than similar tendencies have died in Japan. Even though its grip will weaken, the government will continue to guide the economy, through its influence on *chaebol*.

A commitment to economic liberalisation among some newly-appointed government officials, such as Mr Han Seung-soo, the trade and industry minister, and Mr Cho Soon, the deputy prime minister, will not compensate entirely for the instinctive bias of old hands towards the interests of the *chaebol*. "Korea will remain a tough place for foreigners to do business," says a western trade official.

Also, exports are bound to remain a vital source of growth, even if a declining one in importance. Exports totaling \$21bn last year accounted for a full 35 per cent of Korean gross national product - and they have to keep expanding if only to cover Korea's growing desire for imports.

However, Korea has reached the point at which it has to expose companies to international competition, partly because of US pressure and partly because of self-interest: it wants access to cheap labour, technology and markets. Korea will, moreover, have to move faster than Japan because the West is much more aware of the might of Asian competition than when Japan embarked on its internationalisation some 20 years ago.

"Our national industries have to become international," says Mr K S Lee, executive vice-president of Samsung, a chemicals-based conglomerate. "That will be a fundamental trend from now on."

Rising labour costs provide the main impetus for overseas investment, followed closely by trade frictions. Businessmen believe that Korea may never again be a low-wage economy, following the 100 per cent increase in costs in US dollar terms since 1985. So labour-intensive industries are moving production overseas, particularly to low-wage Asian countries.

As for developed countries, Koreans intend to follow the same route as the Japanese - making themselves at home in export markets: "We must become an insider in target markets," says Mr Lee Chung Suk, an executive director of Lucky-Goldstar.

From an accumulated total of \$47bn at the end of 1985, overseas investment reached \$1.1bn by the end of last year. Samsung, with the most developed foreign investment programme, currently has 5 per cent of its electronics production abroad. In three years' time it plans for between 25 per cent and 30 per cent.

Groups, which had scarcely heard of corporate finance five years ago, are considering mergers and acquisitions. Sammi Steel, a specialist steel maker, recently bought three

units of Rio Algom, the Canadian resources group, for \$210m, in the first significant Korean overseas corporate acquisition. Given rising labour costs, salvation at home for Korea lies in continuing investment in capital-intensive industries.

There is no shortage of schemes, only of capital and technology. There are no less than five competing plans for \$1bn-plus petrochemical complexes.

Korean companies are seeking foreign partners more keenly than in the past for these immense projects. The Government has eased regulations governing inward investment. Foreign investment in Korea is expected to increase from the current accumulated total of \$6.8bn, albeit more modestly than outward investment.

Inward investment has long been regarded as a double-edged sword. Koreans have always desired technology but they have feared becoming too dependent on foreign knowledge. For their part, foreigners have been afraid of divulging secrets to a potential competitor. "Toshiba knows that our ultimate goal is to beat them," says Mr Suh Jung Sun, a senior executive of the Daewoo group, which includes cars, electronics and financial services.

However, both sides have started looking slightly more favourably on partnerships. Foreign companies which once regarded Korea as an export base are now interested in its fast-growing domestic market. Koreans are more aware than ever of their technological weaknesses.

Each advance by a Korean company tends to expose gaps elsewhere: "We have grown so fast we could not accumulate technology," says Mr Lee Eye Sik, a senior official of the Economic Planning Board. Between 20 per cent and 30 per cent of the value of a Korean-made video recorder is imported from Japan. The same is the case for a Korean car.

The main criterion for liberalising inward investment is usefulness to Korea. This is particularly clear in financial markets. Korea is proud of its plan to open its stock market to foreigners in 1992. But since Korea has no particular need of foreign shareholders, the amounts of stock foreigners can buy even after 1992 will be tightly restricted.

The Korean financial system, especially banking, remains under the control of the Ministry of Finance and the central bank. So the liveliest developments involving Korean companies are taking place in international financial mar-

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Editorial production: Khozem Merchant	

kets, especially innovative issues of Europaper.

Nowhere does Korea boast of its commitment to internationalisation more than in trade - not surprisingly, given US criticism. Korea this year narrowly escaped being named on Washington's list of nations accused of unfair trading, under the terms of the "Super 301" clause of US trade law.

US officials concede that Korea is opening markets, albeit cautiously. The Korean list of banned items, as defined under the General Agreement on Tariffs and Trade (GATT), has fallen from 40 per cent to about 1 per cent. The government has cut the average level of duty on imports from 19 per cent last year to 13 per cent. It intends to reduce this to 7.5 per cent, the average for developed countries, by 1993.

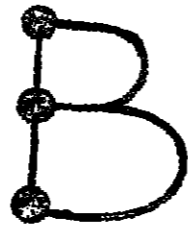
Nevertheless, the end of formal barriers often reveals hidden ones. Since the tobacco market was opened last year, the importers' share of the Korean market has reached 4 per cent. Starting from the same point in Taiwan they have captured between 16 per cent and 17 per cent of the market. The importers blame various restrictive practices by the Korean state tobacco company - including bullying shopkeepers to tear down advertisements.

There is a danger that change is coming so fast that it might overwhelm Korea. Its move to democracy is so recent, its economy is in many ways so immature. But the difficulties of the present are dwarfed by those which Korea has already overcome. Like Japan and unlike Argentina, the bet is that Korea will complete the long journey to economic modernity.

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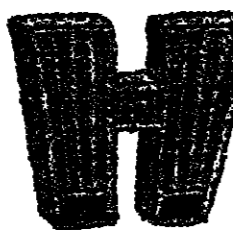
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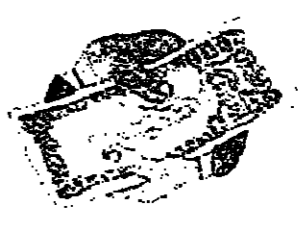
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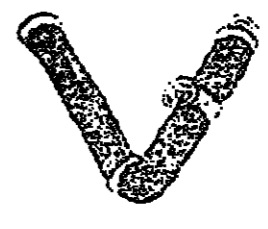
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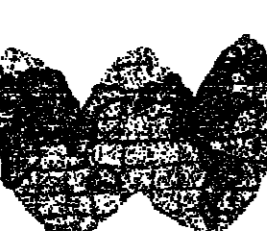
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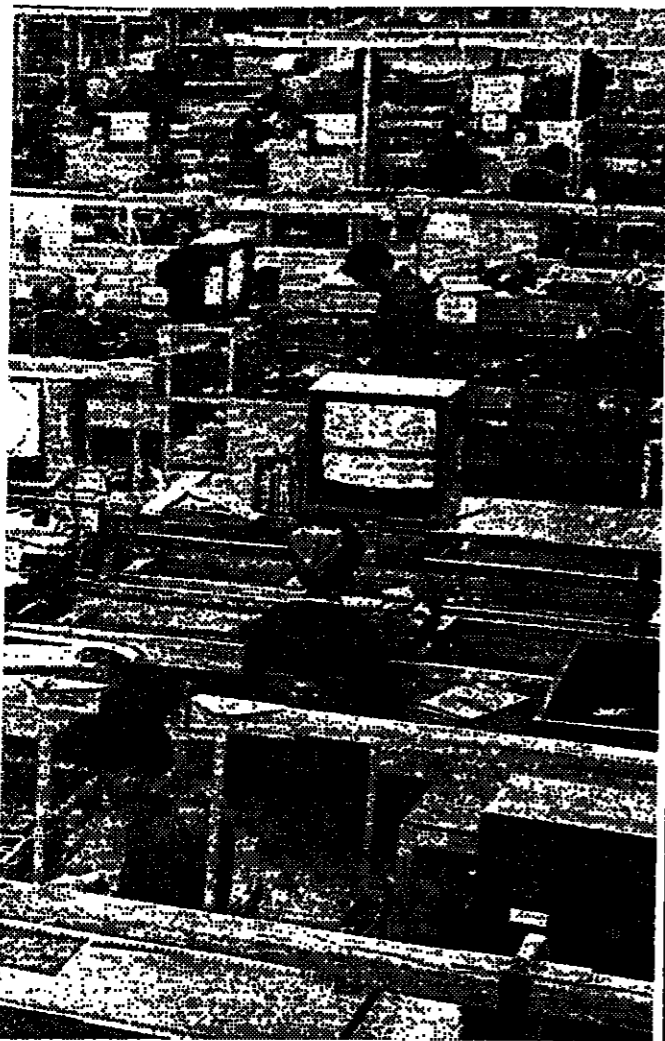
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**SOUTH KOREA: FINANCE & INDUSTRY 2**

Maggie Ford on an economy forced to confront the problems of maturity

**Increasingly fraught growing up pains**



Many South Korean companies are looking to move production of labour intensive products abroad to lower wage countries

IT HAS undoubtedly been difficult for the dynamic South Koreans to adjust to the reality of having a more grown-up, mature economy. All year long there have been outbursts of panic and prophecies of doom predicting the end of the country's economic miracle.

After three years of growth at 12 per cent and last year's current account surplus of \$14bn, the prospects this year

of 6.5 per cent growth and a current account surplus of \$8bn have seemed like failures.

But Seoul is not so much headed for failure as undergoing an economic restructuring. The results of the change will determine its future success in the global market and its status as a leading industrialised country in the next decade.

The restructuring affects both the macro and the micro

sectors of the economy. On the macro side, South Korea has been forced to react to strong trade pressures, especially from the US.

Companies are moving from the strongly export-led engine of growth that has propelled the economy to concentration on a balance between the domestic and international markets.

They are simultaneously try-

ing to move their export dependence away from US markets to a balance between North America, Asia and Europe, and to reduce their import dependence for components on Japan.

Companies also want to upgrade their technology, move production of labour intensive products abroad to lower wage countries, and sort out a working relationship

between management and labour.

In addition, they are facing competition from imports in the domestic market for the first time, as the government lowers tariffs and lifts bans on restricted items.

On the micro side, the Government is planning to introduce a full scale modern tax system, so as to curb speculative activities in property and the stock market. It is expanding welfare and housing spending, and is trying to correct regional wealth imbalances which have arisen during the rapid development of the past. The first ever budget featuring public spending in the history of the country was introduced this year.

It is lifting controls on industry under which government planners "picked winners" and allocated resources to help them in the drive to industrialise.

The result of this widespread restructuring has so far been patchy. Some companies have been quick to grab opportunities offered at home, neglecting their exports in the more competitive environment caused by the 25 per cent appreciation of the currency over the past three years.

Others have invested strongly in speculative assets rather than manufacturing facilities, pushing down the rate of growth but creating inflationary pressure. Speculative activity is expected to ease when a government reform bill takes effect after this year.

Many companies are still working out strategies of internationalisation as South Korea looks to become an advanced economy.

Expected to act in a more independent fashion rather than rely on government guidance, as in the past, they may still not be certain of their future plans.

Most government economists believe that this year's slowdown in growth was necessary to control inflationary pressures. The inflow of funds from the current account combined with wage rises averaging 20 per cent a year over the past three years could have caused a wage price spiral if it had been not checked, they believe.

The central bank has therefore exercised strict control on the money supply this year, resulting in a sluggish stock market. It has also kept interest rates high and strictly rationed lending, especially for speculative purposes.

After strong pressure from industrialists late this year, the Government has lifted some controls in an effort to encourage companies to expand their export effort. Exports grew 4 per cent in 1988 compared with import growth of 19 per cent, mainly in capital goods.

The inflationary pressure is expected to result in a rise in the consumer price index of between 6 per cent and 7 per cent by the year end, a rate which the Government hopes to reduce next year. A current account surplus of \$8bn is now forecast, with a similar out-turn expected next year. The won has depreciated slightly against the US dollar from its high of 870, but no significant further fall is expected, and US officials are reported to be happy with South Korea's progress on trade issues.

The main priorities for the Government next year will be the introduction of a workable system of labour relations to avoid the damaging disputes of the past three years, along with the continued restructuring and modernisation of the fiscal system. The rebalancing of the economy between exports and domestic demand and the introduction of a more competitive approach by companies, both internally and externally, will also be emphasised.

Officials believe South Korea will soon start to experience the advantages of a more democratic and accountable economic system, side by side with political change. Much of the pent-up anger and volatility which has plagued business activity, especially industrial relations, will then begin to moderate, they hope.

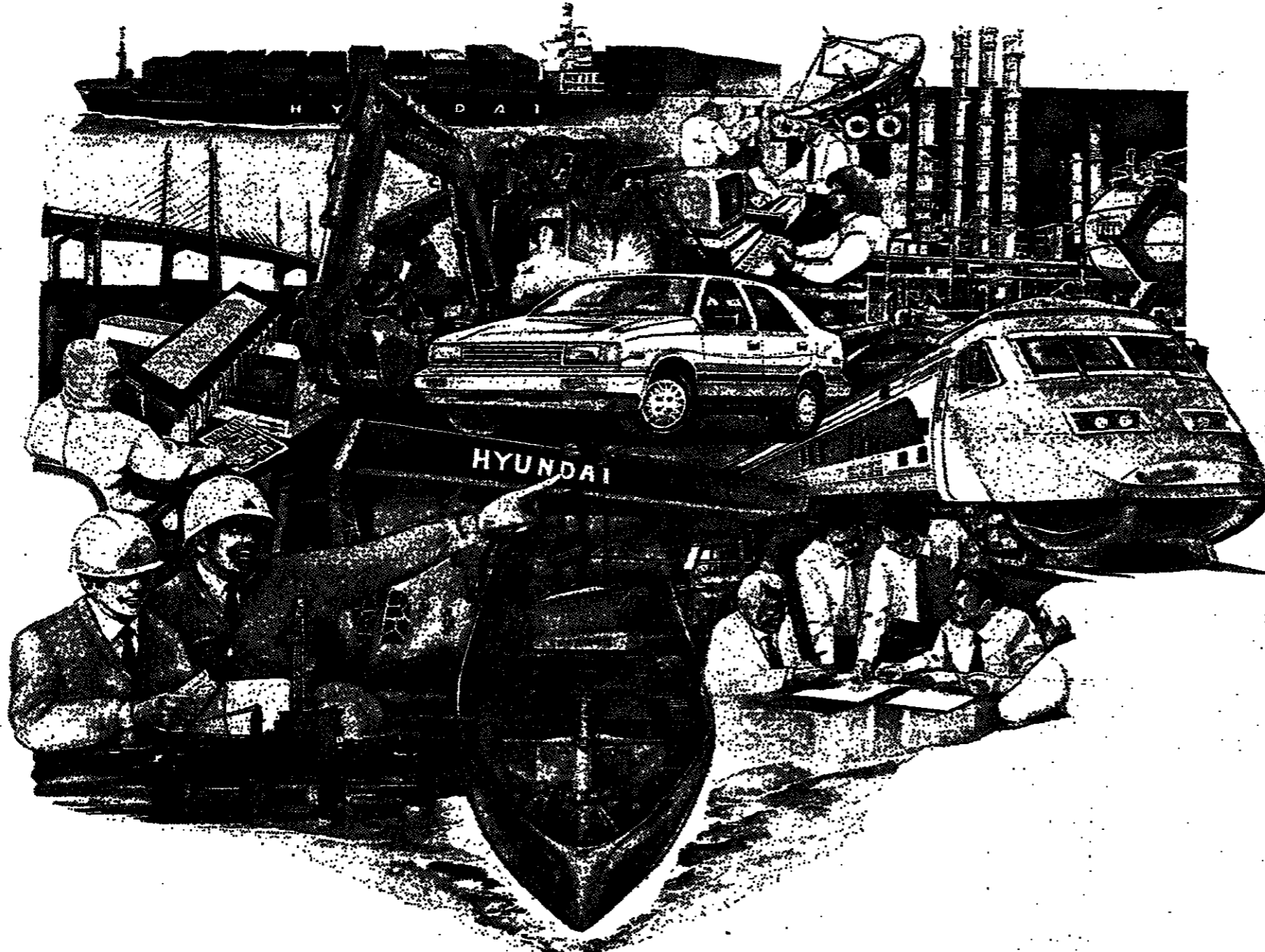
Expectations are also likely to become more realistic. The day may not be far off when South Koreans realise that the achievement of 6.5 per cent growth would be regarded by almost any advanced country as an excellent performance.

Comparative economic indicators 1988

	Korea	Taiwan	Japan	US
GNP current prices (\$bn)	188.2	119.7	2,859.7	4,883.1
Per capita GNP at current prices (\$'000)	4.0	6.0	23.5	18.5
Average annual growth rate of Real GNP 1979-88 (%)	7.0	8.1	4.0	2.5
Average annual rate of change of GNP deflator 1979-88 (%)	9.0	5.3	1.9	5.6
Average annual rate of change of consumer price index 1979-88 (%)	9.3	5.0	2.6	6.1
Annual average rate of change of money supply (M2) 1979-88 (%)	20.0	21.3	8.6	8.1
Unemployment rate (%)	2.5	1.7	2.5	6.2
Current balance as (% of GNP	8.4	8.5	2.8	-2.8
Share on investment in GNP (%)	30.2	28.3	30.7	17.7
Domestic savings rate (%)	37.7	36.3	33.7	18.8
Population (m)	42.0	19.9	122.3	243.8
Average annual growth of pop: 1979-88 (%)	1.3	1.6	0.7	1.0

South Korea Economic Planning Board

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South Korea: economic growth indicators (%)

	1986	1987	1988	1989	1990*	1991*
GNP	12.9	12.6	12.2	8.5*	-	-
Manufacturing	18.4	18.3	18.0	5.1*	-	-
Services	11.5	12.1	11.2	6.5*	-	-
Private consumption	7.8	8.3	8.5	10.2*	-	-
Fixed capital formation	10.0	17.4	11.8	11.2*	-	-
Machinery/equip	21.1	21.3	20.4	7.6*	-	-
Construction	3.4	14.0	13.3	14.5*	-	-
Real GNP	-	12.8	12.2	5.6	7.0	7.5
Export volume	-	28.7	13.0	-4.3	4.5	6.0
Import volume	-	20.9	14.3	9.6	7.9	7.4

\*Jan-June, forecast. Source: South Korea Economic Planning Board

TVs for export: Some Korean companies are now trying to broaden their export markets in favour of Europe and Asia. Below, industrial giant Hyundai which has had to secure state aid to end a damaging two-month strike at its shipyard at Ulsan



**SOUTH KOREA: FINANCE & INDUSTRY 3**

Stefan Wagstyl on the need for reform of the financial system

**Seoul's old habits die hard**

KOREAN finance has an impressively modern facade. Gleaming skyscrapers in Seoul. Bankers and brokers with offices in London and New York. Eurobond issues. Even a \$200m international acquisition.

But behind this screen, there is a ramshackle mixture of old and new elements, unevenly fitted together. In ways which have great muffled gaps in the needs of many Koreans. In some parts of the countryside, there are no banks, small and medium-sized businesses often find it impossible to borrow, and money markets are so undeveloped that the cost of borrowing is anything from 11 per cent to more than 50 per cent.

The core of the system are banks, which were established in order to channel funds to industry at the state's behest, and which are still tightly controlled by the authorities. Around them have grown other kinds of financial company - including short-term finance companies, securities companies, and life insurers - which are mostly expanding rapidly. The banks' share of the financial community's assets has fallen from about 75 per cent 10 years ago to about 50 per cent.

The Government is publicly committed to reducing bureaucratic constraints and allow free market forces greater play and to respond to US pressure to allow foreign companies more access to Korean markets.

Mr Kim Kim, the governor of the Bank of Korea, the central bank, says the purpose is to promote competition and bring financial services to provincial centres, since many of the new institutions will be based outside Seoul.

The central bank has also supervised an important reform of the money market, by unifying two separate illiquid and inefficient call markets, and allowing various financial companies, including foreign banks, to use it. The deregulation of interest rates on deposits is on the agenda, possibly starting next year.

For the future, President Roh Tae Woo has endorsed a liberalisation plan which set a date of 1992 for the reform which is highest on the wish-list of foreign companies - the opening of the securities market to overseas investors by 1992. There will be tight limits set on the proportion of shares foreigners can buy.

The convertibility of the won, indispensable for freedom of capital, is to move ahead in stages. This year, banks were allowed to set their own rates for telegraphic transfers (within a narrow range), next year the market average rate system as used in Taiwan is to be adopted for setting exchange rates, and at an unspecified date after 1992 the won will be made fully convertible.

None of this is happening fast enough for the securities companies, which have seen the Korean stock market exceed Hong Kong in total capitalisation in the past year. About 125 companies have been listed this year, taking the total to 690. Listings are expected to continue at the same rate as the conglomerates are being pressed by the government to spin off

their subsidiaries to spread ownership. The securities companies have followed banks in establishing overseas offices - principally to manage and underwrite issues of Korean companies on the Euro-markets. They complain that the Government has not allowed the market to grow freely. About a dozen issues by Korean companies were expected this year after five in 1988. However, there has only been one so far, with two more planned by the end of the year. The government blocked other issues out of concern about the growth of the domestic money supply (the proceeds of overseas issues often find their way back into Korea, in spite of foreign exchange controls).

Nevertheless, the Government discreetly encourages Korean financial companies to get involved overseas in complex transactions. Like the Japanese authorities, the Koreans want to see their companies learn techniques abroad before allowing them to be used at home.

With the help of foreign securities companies, Korean houses are handling increasingly sophisticated deals, for example, the single Eurobond issue launched so far this year was a \$50m bond with warrants for Sammi Steel, a specialist steel maker, co-managed by Merrill Lynch, the US broker, and Dongsub. Sammi is using the money for a \$200m acquisition of three subsidiaries of Rio Algom, the Canadian mining and metals group, in the first significant international acquisition by a Korean group.

Banks too are expanding corporate finance operations. The Korea Development Bank, the state-owned long-term credit bank, is developing an international investment banking operation. It has \$21.5bn in assets. Mr Chung Yung Hui, the governor, says he wants to model the bank on the Industrial Bank of Japan, Japan's premier long-term credit bank.

Such comparisons are bold, considering that the privatisation of the KDB is not even on the agenda. However, the authorities are aware that true competition can only flourish if Korean institutions are ready to stand on their own two feet.

The leading commercial banks, which were mostly privatised in the early 1980s, are being encouraged to raise capital to meet capital adequacy standards set by the Bank for International Settlements. According to the central bank, seven out of Korea's 17 banks failed to meet BIS standards. Most of the seven have high exposure to bad loans they were prompted to make to heavy industry by the government during the 1970s. The central bank is pressing banks to write these loans off over time against earnings. It believes Korean banks can meet BIS standards by the date they come fully into effect in 1992.

Korean companies will be exposed to the full blast of competition only when they can stand it. And even then, as independent companies, they will be expected to relate closely to the authorities. Just as in Japan.

**The Government is publicly committed to reforming the system in order to reduce bureaucratic constraints and allow free market forces greater play**

EXPORTERS to South Korea, rushing to take advantage of market opening measures and tariff reductions, could lately be forgiven for wondering exactly what kind of country they are dealing with.

In the past few months a perfectly respectable grapefruit market, which had grown from nothing to several million dollars worth of imports in a few months, was virtually destroyed overnight.

A fast growing imported film business launched by an American company was subjected to a barrage of intimidation, including the release of snakes in cinemas to deter movie-goers and cinema owners.

A scandal over the use of imported ingredients which might be harmful to health in locally manufactured noodles created an overnight boycott of one of the country's staple foods.

And a campaign was launched against excessive consumption in the South Korean press which seemed to focus largely on the kinds of high priced, high margin goods that exporters have found highly profitable to sell in Asia, especially Japan.

Just what was going on, many importers wondered, thinking darkly that they were probably the victims of another stab in the back from local vested interests.

Many foreign businessmen in South Korea believe that local companies, whether government-backed or independent, are determined to prevent competition in a domestic market which has been heavily protected for decades.

However, the reality of the situation may be more complex. For while there are undoubtedly some political and unethical business aspects to recent events, foreign companies' business judgment may be better served by watching social change and the volatility of public opinion.

A wave of political and social discontent has recently broken throughout South Korea as the country's dynamic material success collides with traditional values.

Public protest has concentrated on the conspicuous consumption of luxury goods by the rich, and concern has grown about the spread of corruption. The underlying reason for the complaints is the uneven distribution of the nation's new wealth.

A recent poll showed that a majority of the public felt that the distribution of income in South Korea was unfair, and that it was wrong for a small minority to indulge in excessive consumption of expensive luxuries denied to the majority.

The debate about consumption has focused on imported goods, especially foreign cars, drinks, and consumer items such as TV sets and other home appliances and designer clothes.

It has particular relevance for exporters trying to break into a market which until now has been tightly restricted to domestic manufacturers.

Newspapers have chronicled the increasing rise of imports of very expensive products such as chandeliers, marble bathroom fittings, furs and jewellery, along with high spending at entertainment places, where a night out can cost several hundred dollars per person.

But government officials say that the discontent which has been fanned by the media is not an anti-import campaign. The policy to open South Korea's markets is not in jeopardy, they say, pointing to high profit margins on luxuries as the cause of the trouble.

Newspapers have published analyses of the profit margins, often as high as 200 per cent on imported items, noting that the cost of imported products in South Korea is often quadruple the cost in the home country.

**IMPORT LIBERALISATION**

**The growth of consumer power**



Taste of things to come: South Korean housewives protesting against the import of farm products, including US grapefruits

Big business groups, which own the trading companies bringing in imported goods, have attracted strong criticism, not only for the high profits charged on items which are reasonably priced abroad. They are also under attack for indulging in speculative investment in property which drives up housing costs and for trying to dominate all business fields by squeezing out smaller companies.

The result of this activity has been a concentration of wealth in a small upper echelon, which clashes with the Confucian value of egalitarianism so common in north-east Asia.

The Confucian tradition emphasises respect for hierarchical authority, but it also stresses the duty of rulers to treat people fairly. Scholarly distinction and frugal living are venerated. Materialism, until very recently, was practically unknown in Confucian societies and being rich was not regarded as deserving of respect.

South Koreans have observed the development of the wealth gap in a more extreme form in neighbouring Japan, where speculators and large companies have scooped up financial assets such as land and stocks, putting home

ownership out of the reach of many salary earners.

They are also starting to notice the wide disparity between prices for goods overseas and at home, having been allowed to make foreign trips for the first time this year.

South Korea may, however, have the best chance of the north-east Asian countries of tackling the wealth gap problem.

The Government has already announced that it will introduce a tax and land reform programme, including a modernised stock market system using real names in transactions, so that speculators can be taxed on profits.

The Government also seems to be approaching the question of high profits. The issue has been underlined by the release recently of figures showing margins of up to 200 per cent on "luxuries" - which in South Korea may include such relatively commonplace items as a melon selling for £10, or a bottle of Scotch whisky for £33.

Ministers say that imports of foreign products are being allowed to go as to introduce competition into the domestic market to upgrade quality, as well as in response to foreign trade pressure. They are critical of companies who are using open market opportunities simply as a way of making what they see as exorbitant profits.

The growing consumer movement in South Korea has also shown its muscle by forcing department stores to stop making false claims on prices during bargain sales, and by making public complaints about food testing standards.

But for exporters, the market remains difficult to judge. Like most developing countries in Asia, many South Korean consumers with money to spend feel that the more expensive, the better the quality, and therefore the more desirable the product.

Any manufacturer or distributor reducing product prices may therefore sacrifice profits in the short term - though in the long term he may gather public loyalty and consumer support for his product and his sales policy.

In a Confucian-style society such as South Korea, it is becoming clear that getting rich and spending money is not necessarily always regarded as glorious. In gaining maximum profits and long-term market share, timing will, as usual, probably be the essence of success.

Maggie Ford

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**SOUTH KOREA: FINANCE & INDUSTRY 4**

Maggie Ford on the rising tide of shop-floor unrest

**Unions stake their claims**

IN THE next six months South Korea will face two substantial challenges to its desire to become an advanced industrial country with a democratic political system.

The first is the need to come to terms with its past, and especially to eradicate the still festering legacy of the previous government led by ex-President Chun Doo Hwan.

The second is the need to set up a modern relationship between management and workers to end the destructive strikes and high wage rises of the past few years, which have eroded international competitiveness.



President Roh Tae Woo

Serious obstacles lie in the way of a resolution to the twin problems, but confidence is now beginning to grow in the country's ability to find speedy solutions.

Negotiations have now been going on for two years between ruling and opposition parties over a settlement of the misdeeds of the former government. A year ago former President Chun apologised to the public for his actions, returned substantial funds to the state and departed for internal exile in a remote Buddhist monastery.

The opposition has, however, stuck by its demands that he testify to the National Assembly about his actions. Several other key figures in his regime are also required to resign from their present positions.

Victims of the 1980 military killings in the city of Kwangju must also be compensated and their reputations restored, in order for a settlement to be agreed. Ruling party officials now seem close to negotiating terms with the leaders of the previous government, observers believe, and a peaceful solution is expected to be found within the next few months.

The Government of President Roh Tae Woo will then be in a far better position to push ahead with its policies, which have often attracted strong opposition from hardliners associated with President Chun.

One such policy concerns the future of the labour movement, which sprang up three years ago in the wake of the 1987 democracy demonstrations. Workers in South Korea reacted strongly to democrati-

among workers in competing companies.

Wages as a percentage of costs in South Korea still remain at between 15 per cent and 20 per cent, so that in high value added industries such as motor cars, the country remains competitive, other factors being equal. Managers say that stoppages and production delays due to disputes at suppliers are causing the most damage.

The Government has remained neutral in many disputes but has allowed police to intervene in others, creating substantial distrust. It has made it clear that it wants a unified trade union structure, led by the Federation of Korean Trade Unions, and plans to crack down on a grouping of democratic trade unions formed earlier this year.

Mr Kim Woo Chong, owner of the Daewoo Group, whose shipyard was bailed out by the Government this year, may be moving towards acceptance of such a point of view.

Last year, after serious violent labour strife at the yard, he acceded eventually to demands from the trade industry that he personally sort out industrial relations as a condition of financial aid for the yard.

Mr Kim spent six months on the site, finding time to write his autobiography. Last month a delegation of trade union officials from the shipyard was sent at Daewoo's expense to Poland, where they are to meet Mr Lech Walesa, the Solidarity leader, and his colleagues at the Lenin shipyard in Gdansk.

No doubt the two groups of workers will find their beliefs in democracy to be much the same, though clearly the state of the country's economies could not be more different.

At the same time, other trade union leaders are travelling to western Europe and the US to look at industrial relations, and the Government is to set up an education and training centre at the FKIU for union officials.

Next year's wage round may see a watershed in South Korean industry, where the principle of unions is fully accepted by management, and the formation of representative unions is encouraged.

The outlook then will be bright, for South Korean workers' vitality is expected to remain undimmed so long as they are rewarded fairly for their undoubted contribution to the country's prosperity.

of industrialists. Some industrialists, unions leaders say, believe that workers should be grateful to have a job at all.

The Government has moved to improve the macro-economic situation for workers by introducing welfare spending in the budget, reorganising the fiscal system and cracking down on speculation by companies in property, which was driving up home prices beyond the reach of workers.

It has also warned both sides that it will not tolerate violence and that both workers and management should realise they are in the same boat.

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**Seoul is no longer a low cost export base, writes John Ridding**  
**High labour costs deterring potential foreign investors**

AS THE Korean economy adjusts towards greater emphasis on domestic demand and more capital intensive production, so the incentives and opportunities for foreign investors are being transformed.

Whereas in the past foreign investors regarded South Korea as a low cost export base for cheap consumer goods the main attraction today is increasingly the domestic market and the potential for exporting higher value added products.

One of the principal factors in this change has been the sharp increase in production costs over the past few years. "Costs have advanced by leaps and bounds," says Mr Richard Lalber, co-chairman of the investment committee of the US chamber of commerce. "The days of cheap labour are over."

Not only have wages soared over the past two years as Korean workers have demanded their share of the country's economic success, but working hours have also been reduced. As a result, estimates Dr Jung Sun Suh of the Daewoo Research Institute, unit labour costs have advanced by as much as 40 per cent over the past year.

The impact on costs has been amplified by currency movements. Although the won is unlikely to appreciate by more than 2 per cent against the US dollar this year, it remains more than 20 per cent higher than its 1987 level.

In addition, wage demands and calls for union recognition have often been accompanied by strikes. Foreign companies have suffered at least as much as domestic organisations and in a number of cases there has been a strain of anti-Americanism.

The combination of these factors has certainly had an effect. In the first nine months of the year total new foreign investment fell from \$1.09bn to \$864m, a decline of about 20 per cent. Several existing investors have also pulled out of Korea. National Semiconductor and Tandy of the US, for example, both found it increasingly difficult to maintain sufficient profitability from their relatively labour intensive electronics businesses. Similarly, five of the 70 companies at the Masan free export zone have withdrawn their investments so far this year.

But as the incentives for export oriented investors recede the attractions of the domestic economy are increasing. The flipside of the higher wages being paid to Korean workers has been a sharp increase in domestic consumption. The Korean market, with 43m people and a per capita gross national product approaching \$5,000 provides a valuable source of demand.

In the longer term many investors believe that Korea will be second only to Japan among the economies of the region and that it will provide a good base from which to export to other Asian economies.

From the Korean side there is a need for individual companies and the economy as a whole to gain access to more advanced technology. This is necessary to retain international market share from regional and lower cost competitors but is expensive and slow to develop domestically.

Where the incentives on both sides meet several substantial foreign investments have resulted. Volvo, the Swedish car manufacturer, recently signed an agreement with Saangyong, a Korean counter-

**Foreign investment trend by country (on approval basis; \$'000)**

	1987		1988		1989*		Total 1982-89	
	Projects	Amount	Projects	Amount	Projects	Amount	Projects	Amount
US	93	255,140	104	284,401	72	282,843	892	1,874,948
Japan	207	493,899	177	696,244	99	383,035	1,676	3,425,236
Hong Kong	8	45,880	4	18,235	5	22,584	39	213,274
W. Germany	10	41,493	15	74,040	17	38,574	59	215,855
UK	6	46,228	8	21,781	7	39,191	45	174,650

\*Jan-Sep

Ministry of Finance

**Foreign investment trend by sector (on approval basis; \$'000)**

	1987		1988		1989*		Total 1982-89	
	Projects	Amount	Projects	Amount	Projects	Amount	Projects	Amount
Agr/Fisheries	1	2,747	1	9,847	1	2,158	80	35,165
Manufacturing	323	779,245	273	738,174	143	583,196	2,450	4,405,413
Chemicals	45	153,401	44	287,471	22	145,408	306	991,148
Machinery	48	87,645	82	84,972	29	70,082	407	396,182
Electronic products	80	212,157	55	288,884	28	90,587	547	1,099,882
Transport equipment	31	119,532	12	43,193	11	142,850	113	943,239
Services	35	277,158	65	833,085	94	293,560	419	2,385,956
Hotels	6	246,877	5	418,502	2	66,689	76	1,695,191
Financing	1	16,080	7	98,787	3	111,005	33	387,692

\*Jan-Sep

Ministry of Finance

part, to produce a Volvo model in South Korea and to jointly develop a new car. ICI, the UK chemicals group has two investments in Korea, one of which supplies chemicals with a high technical content for use in quality textiles.

For Mr Robert Milligan, President of ICI Korea, the operating costs are not the principal issue. "We haven't come here because of cheap labour. We are here because we believe long term it is going to be an innovative economy and will play a significant part in the region."

Because of its desire to attract high-tech investment the Korean government has retained tax exemptions for products or processes which it places in this category. In addition, new guidelines for foreign investors, issued in July, have smoothed the process of investment applications, guaranteeing that a decision be taken within 60 days and eliminating requirements to export a given amount of output.

Most important, however, is the gradual liberalisation of new business areas to foreign capital. Following an agreement in May between South

Korea and the US several manufacturing and service areas, including pharmaceuticals and advertising, are now open to foreign joint ventures or 100 per cent ownership.

But in spite of these measures and the attractions of the Korean market, investors still face an array of disincentives. For Mr Michael Jackson, the British commercial counsellor in Seoul, the most important has been the frequency of strikes and labour disputes. He believes that the next wage

same access to Korea's banks enjoyed by local counterparts.

In addition, there are complaints that in spite of official liberalisation measures, new or changing regulations often make it difficult to take advantage of the opportunities. When, for example, trading companies were allowed to be set up tight capital restrictions continued to provide an obstacle. Furthermore, Mr Milligan argues "it is still extremely difficult to make a 100 per cent investment even in the permitted areas."

But the Government has shown itself to be responsive to foreign concerns. At the beginning of the year, foreign companies, supported by US officials, campaigned against a requirement that all Korean companies satisfying certain criteria, including joint ventures and other foreign investments, should float on the stock exchange. They argued that control would be diluted and that it was unfair for such requirements to be retrospective.

In the event the Ministry of Finance accepted that the "going public" requirement should only apply to investments made after December 1988 and after the companies had been operating for a three year period. "The issue is now on the back burner," notes Mr Jackson. "I don't think it represents a serious disincentive, although it may crop up again at the end of the three year period."

By then, the total level of direct foreign investment in Korea should be comfortably ahead of the current \$6.8bn. How much ahead is hard to predict, although Mr Kim Kyo Shik, from the government's foreign investment policy division, believes its will remain at about 3.5 per cent of gross national product.

More certain is his prediction that the type of investment will increasingly be capital intensive, focused on the Korean market, with a growing presence of service industries.

**As the incentives for export oriented investors recede so the attractions of the domestic economy are increasing. The flipside of the higher wages being paid to Korean workers has been a sharp increase in domestic consumption**

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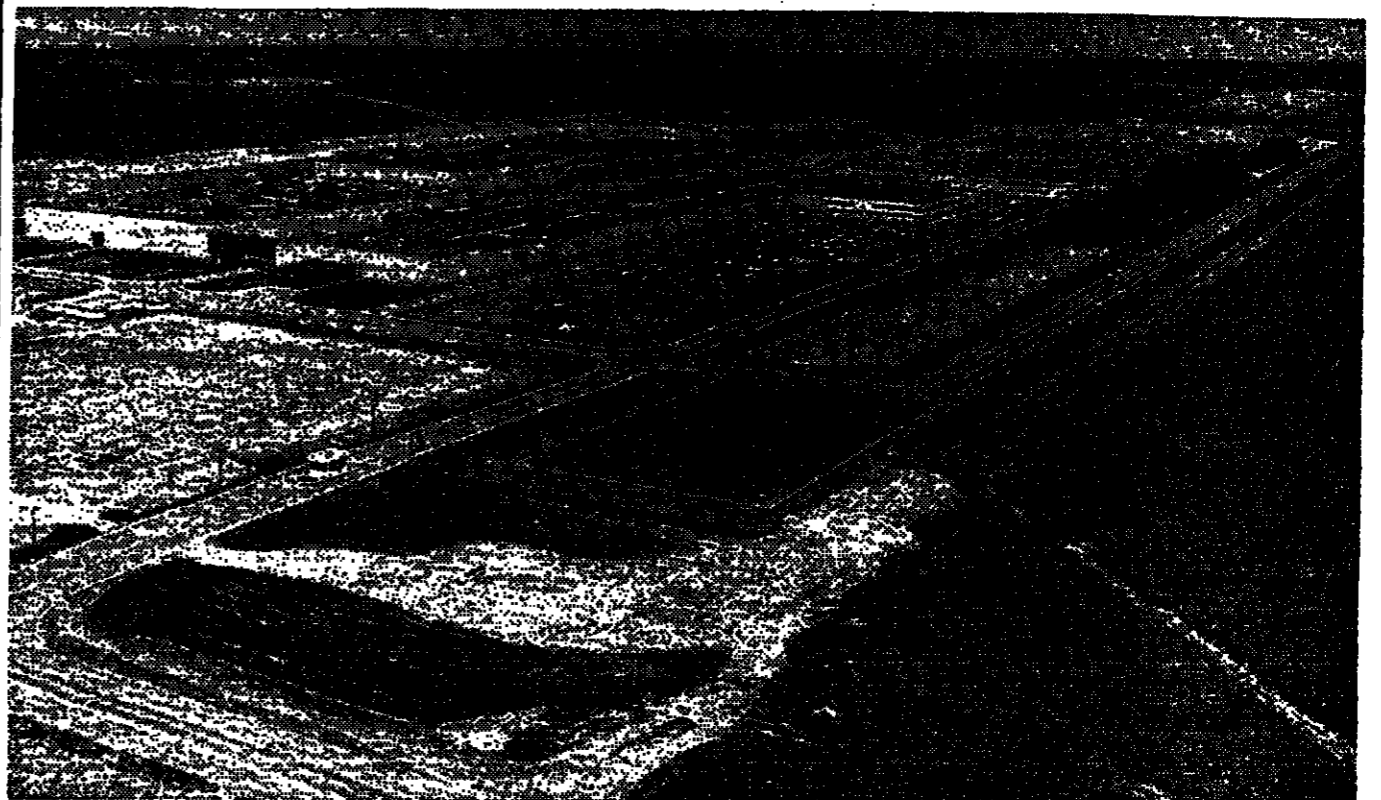
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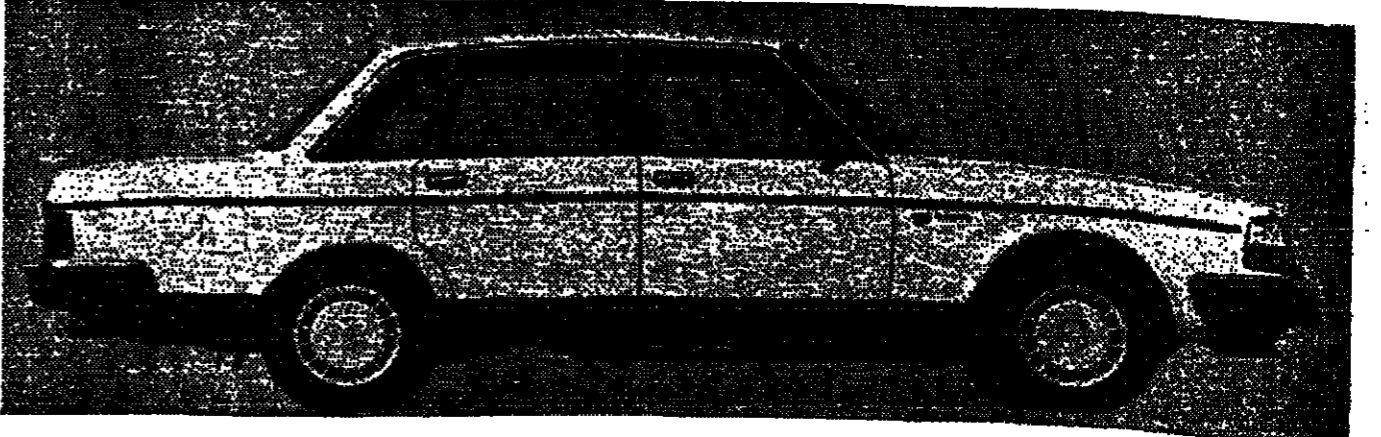


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Foreign ventures: Hyundai's Canadian car plant, one of the biggest single Korean investments abroad. Below, Volvo's 200 series which will be the basis of a new model to be made in Korea with Saangyong. The two companies have signed a letter of intent



**SOUTH KOREA: FINANCE & INDUSTRY 5**

John Ridding on overseas interest in the Korean equities market

**Investors pay high price for exposure**

UNTIL the South Korean stock market is opened to foreigners in 1992, overseas investors who are hungry for exposure to Korean equities can satisfy their appetite only indirectly, through a handful of vehicles traded on the Euro market.

Such limited access, combined with growing interest in the Korean market has prompted high prices for the available paper.

The seven unit trusts have traded on premiums as high as 100 per cent, while the Korea

**The market is already capitalised at \$140bn, making it the 10th largest in the world, and is expected to exceed \$200bn by the time it is opened to foreigners**

Fund and the Korea Europe Fund, two closed end vehicles, and the six convertible bond issues have generally been higher still.

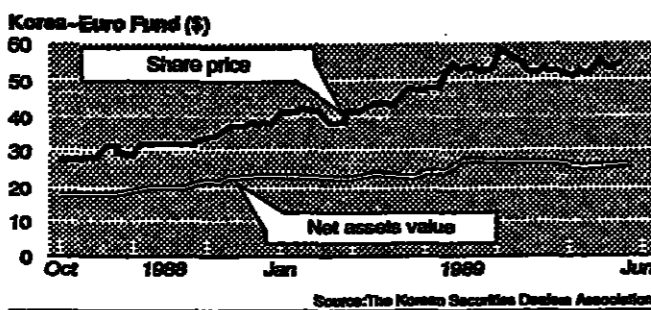
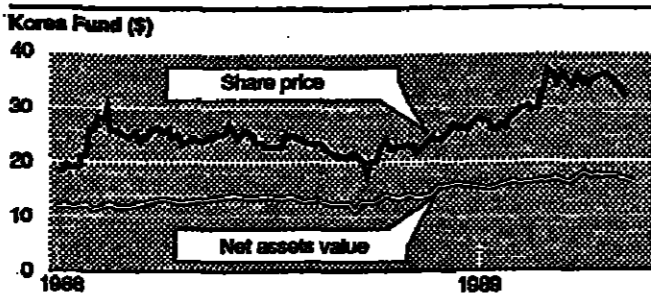
Not surprisingly, such premiums are discouraging to many investors. "We are not prepared to pay that sort of price to get into Korea," remarked the pension fund manager of one large UK company. "We will wait until the market opens before considering any investments there."

But notwithstanding the occasional correction such as occurred following the Tiananmen Square massacre in Peking in June or the falls in international markets in October, the Korean Euro-papers have generally shown steady gains.

"The foreigners who got in early made a lot of money," notes Mr James Williams, a director of Barings International Investment Management, which currently manages more than \$350m of Korean investments. He estimates that "certainly in our first four or five years we made about 12 times our money in dollars."

This year has also seen strong growth. In the first eight months the combined market capitalisation of the various issues increased by 55 per cent compared with seven per cent for the market as a

**Performances of the KF and KEF**



Source: The Korea Securities Dealers Association

whole. Although the Euro issues, like the underlying index, have fallen off since then the total value of Korean paper now traded has grown in excess of \$3bn.

Equally important, however, are the attractions of the underlying market to which some of the instruments will ultimately give access. Although the market has been disappointing this year, with

**Overseas investment vehicles for the Korean stock market (\$)**

Unit Trusts	Price Oct 31 '89	Net asset value Oct 31 '89	Premium (%)
Korea International Trust	104	80.10	73
Korea Trust	124	72.09	72
Seoul International Trust	74.5	43.22	72
Seoul Trust	73.0	41.81	75
Korea Growth Trust	73.5	42.78	72
Korea Small Com Trust	26.0	16.96	53
Korea Emerging Company Trust	27.5	17.21	60

Convertible Bonds	Price (%) Oct 31 '89	Net asset value (%) Oct 31 '89	Premium (%)
Samsung Electronics	987.5	N/A	161
Yukong	322.5	N/A	157
Daewoo Heavy Industries	820	N/A	124
Goldstar	200	N/A	125
Saehan Media	180	N/A	131
Saemil Steel (Warrant)	55	N/A	203

ancing suggest a strong source of demand. Furthermore, the market is relatively stable compared with some of its regional rivals, notably Taipei.

While the various instruments all enjoy substantial premiums their characteristics and performances show marked differences even within the three categories.

The Korea fund, which is approximately three times larger than its European counterpart has relatively good liquidity through its listing in

**Although the high premiums enjoyed by Korean Euro-paper provides a cheap form of finance for Korean companies the outlook for new issues remains unclear**

New York but consequently faces US Securities and Exchange Commission regulations which prevent it from investing in financial stocks.

When this sector performs well, its more aggressively managed London rival has shown more rapid gains.

The unit trusts all have widely varying components with the largest, the Korea International Trust being the most closely indexed. However, the best opportunity for targeting investment lies with the convertible bonds where the premiums reflect perceptions of the underlying quality of the company.

The markets in all of the issues remain tight with daily volume averaging only between \$5m and \$10m. "It is not a country we particularly want to trade," says Mr Williams. "Even when our Korean positions adversely impact on profits we are not prepared to sell out because we are effectively locking money away in a place we regard as sound."

There is also at present little incentive to convert the issues. Some of the earlier instruments are now technically due for conversion but the high premiums would immediately be lost and the proceeds cannot be used to buy other Korean shares until 1991.

Although the high premiums enjoyed by Korean Euro-paper

provides a cheap form of finance for Korean companies the outlook for new issues remains unclear.

The Korean government is committed to a policy of financial liberalisation and a schedule published in 1988 stated that restrictions on overseas issues by Korean companies would be relaxed.

As a result, analysts were expecting about a dozen issues this year as Korean companies sought to take advantage of low cost funding.

In the event, however, the government's concern about excess domestic liquidity and the requirement that funds raised on the Euro markets are used for external projects has resulted in only one issue so far this year, albeit the country's first bond with warrant.

There are signs of an improvement. A \$30m issue by STC, a flexible packaging maker is imminent and will be followed closely by an issue by Korea's second largest construction company. A third tranche is also planned for the Korea Euro Fund.

But until domestic monetary policy is eased and more foreign ventures are forthcoming from Korean investors then there is unlikely to be a substantial increase.

More certain is that the demand for available paper will further strengthen. According to Mr Gavin Roberts of James Capel: "The most potent reason for the rise in premiums this year seems to have been the proliferation of new Asian funds out of Europe and the UK."

Given plans to launch additional funds and the fact that a fixed percentage will be placed in Korean paper the upward pressure on prices will remain.

But as the countdown to market opening continues it is unlikely that the premiums can maintain their lofty heights. "We expect some erosion," says Mr Robert Simpson of James Capel, "perhaps to about 50 per cent by 1992."

But the likelihood that the opening of the Korean stock market to foreigners will initially be on a limited basis and that the underlying index will surge as 1992 approaches, should ensure the market for Korean Euro issues remains strong.

**BARINGS**

**Patience a virtue in a tried and trusted place**

IT IS perhaps surprising that a privately owned and family controlled British merchant banking group has been one of the most active foreign players in the internationalisation of South Korea's financial markets.

But since it first started doing business with Korea in the 1970s Barings has built up a strong position in its three areas of activity.

The merchant banking side has been one of the most widely used issuers of Korean paper, the investment management business is one of the largest holders of this paper, and Barings Securities, which makes markets in all of the Korean instruments open to European investors, is one of the most active traders.

At present, Barings, like all foreign securities companies is restricted to a representative office and all business is conducted offshore. The amount of business is also relatively limited. The past year, for example, has seen only a couple of issues on the Euro markets.

None the less, foreign brokers are mushrooming in Seoul. By the end of this year, about 25 will have established representative offices and all of the big names are already there. The most recent, Salomon Brothers, opened earlier this month. Barings itself has almost doubled its staff in Korea over the last year and now has 18 people in its representative office.

"Competition has certainly become tougher," notes Mr Duncan Ross, Barings Chief Representative in Korea. "Supply is not keeping up with the demand from the foreign houses."

But for Barings as for the more recent arrivals, the main attraction of Korea is longer term and springs from the government's programme of financial liberalisation. In particular, the foreign houses have their eyes on the opening of the Korean stock market to foreign investment in 1992.

"Our basic philosophy is not to make money immediately," says Mr R.Y. Cho, a director of Barings Securities. "We are investing now so as to win the maximum returns when the

Korean stock market opens to foreigners."

Although much can happen between now and then, Barings is confident that the market will have a strong attraction to overseas investors.

"Once the market is opened its capitalisation could represent between 3 per cent and 4 per cent of the world total," estimates Mr Cho. "Investment managers will feel a strong



Family force: the Barings logo

pressure to place part of their portfolios there." However, Barings, which is also active in the other East Asian markets, argues that the Seoul exchange has specific advantages over regional competitors.

Unlike Taiwan, which is biased towards small and medi-

**For Barings as for the more recent arrivals, the main attraction is longer term**

um-sized industry, and Hong Kong which is property oriented, Korea is seen as having a broad range of established industries from steel, to semi-conductors and textiles.

It is also perceived as a relatively stable market. Although this partly reflects the absence of foreigners, who have tended to be fairly quick to sell in Tokyo, it is also the result of government guidance through the institutions. In October 1987, Seoul was one of the few world markets not to fall.

"Korea is a very sound underlying story," says Mr James Williams, director of Barings International Investment Management. "Other emerging markets are going to come and go but this is very much a tried and trusted place."

On the merchant banking side of the business, opportunities are likely to arise from an increased rate of corporate issues and from the development of merger and acquisition activities.

"This field of business is still at a youthful stage," says Mr Ross. "But I believe that Korea will follow a similar pattern to Japan, and more quickly." One reason is a desire to establish overseas plants in Europe to circumvent possible restrictions resulting from the creation of a single European market.

Barings believes that its relatively long involvement in Korea and its position as one of the most active foreign houses will strengthen its hand when these opportunities arise.

Not only will it have developed a research base, but it will be able to advise the Korean government starts to award licences for branch offices, currently scheduled for 1991. In particular, it hopes to gain from the fact that it was the first UK merchant banking group to be allowed to set up a representative office in Seoul.

But competition for the rewards of liberalisation will not come only from its foreign counterparts. Domestic brokers will themselves be seeking to capitalise on the opportunities arising from the internationalisation of their markets.

"The competition from domestic brokers will be much stronger than from the Japanese in the early days of their financial liberalisation," says Mr Sean Gairick, chief representative of Hoare Govett.

"They have large staffs and have long seen the internationalisation of their market as a profitable opportunity."

For the foreign securities companies immediate returns seem unlikely. As in Japan most are likely to find it hard to cover overheads for the first few years.

"I don't think it will be a very profitable source of business from 1992 because of the limited opening," says Mr Cho. "But we are confident about the markets prospects and will be patient."

John Ridding



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## SOUTH KOREA: FINANCE &amp; INDUSTRY 6

Stefan Wagstyl reports on the conglomerates' moves abroad

## The chaebol go international

AFTER years of single-minded commitment to exports, South Koreans are investing in overseas production. They are seeking to build plants in low-wage Asian countries to escape the pressure of spiralling labour costs in Korea and the appreciation of the won. And they need to invest in the US and in Europe to get closer to markets and to minimise trade frictions.

Also, there is increasing criticism in Korea of the dominant role of the conglomerates, or chaebol, in the economy. The top four companies - Samsung, Daewoo, Hyundai and Lucky-Goldstar - account for nearly 20 per cent of manufacturing industry. Foreign investment is a key way for these companies to grow without running into political trouble.

Moreover, overseas expansion will encourage these diversified groups to specialise and so improve their international competitiveness. Samsung, for example, intends to lean increasingly towards electronics.

Foreign investments are complex undertakings for groups which are newcomers to cross-border management. Like the Japanese before them, Koreans have run into clashes of culture which sometimes have undermined the benefits of investment.

Moreover, because international markets are much more competitive than 20 years ago, the Koreans have to move more quickly than the Japanese did when they were embarking on the first stages of their post-war internationalisation.

Korean overseas investment is starting from a very small base. Until the mid-1980s, foreign exchange was so scarce in Korea that the government rarely granted permission to invest overseas. The priority was to earn foreign exchange, not spend it.

But the rapid growth of the current account surplus, to \$14bn last year, has removed much of the reason for restrictions. From an accumulated total of \$476m at the end of 1985 overseas investment soared to \$1.1bn by the end of last year with a further increase of \$200m-plus expected in 1989.

In the first eight months of 1989, 140 cases were approved,

worth a total of \$138m.

As the figures suggest, most investments are quite small in terms of initial investment. But there are already some big exceptions, including the C\$400m car assembly plant opened last year in Canada by Hyundai Motor, an arm of the Hyundai conglomerate.

However, the average size of investment is expected to grow rapidly as companies, for example, increase the size of pilot plants into full-scale factories.

While the first significant overseas investments were made as long ago as the 1970s, big companies are only now beginning to conceive full-scale international investment strategies.

Mr Lee Sun Hak, a senior official of Samsung, which has the most developed foreign investment programme, says: "First you start exporting, then you establish sales companies, then a production base and then a global marketing system. Four stages. We are in between the second and third stage at the moment."

Samsung has seven electronics factories overseas and plans nine more in the next two years. Currently, 5 per cent of production is abroad, in three years' time it will be between 25 per cent and 30 per cent.

South Korea's leading business groups		
	Sales	Activities
Samsung	\$31bn	Electronics, semiconductors, aerospace, food, retailing, shipbuilding, insurance, hotels, trading, paper
Hyundai	\$27.8bn	Cars, shipbuilding, electronics, semiconductors, construction, heavy machinery, financial services, retailing, trading
Lucky Goldstar	\$22.8bn	Electronics and semiconductors, telecom, chemicals, refining and petrochemicals, trading, financial services
Daewoo	\$15.2bn	Heavy machinery, cars, textiles, aerospace, electronics, telecommunications, financial services, hotels
Sunkyoung	\$9.3bn	Refining and petrochemicals, textiles and polyester products, trading
Saangyoung	\$8.3bn	Cement, construction, cars, financial services, resorts
Hyosung	\$4.2bn	Textiles, heavy machinery, trading
Hanjin	\$4.1bn	Transport, air (Korean Air) sea and road, hotels
Kia	\$3.7bn	Cars
Korea Explosives	\$3.4bn	Petrochemicals, hotels and resorts, financial services

Source: Bank of Korea

The importance of the US market is highlighted by the fact that North America accounts for 43 per cent of accumulated external direct investment - boosted by Hyundai's Canadian motor plant.

Europe accounts for only 8 per cent, a figure Koreans would like to see increase. Korean businessmen have neglected the European market for a long time since they judged the US easier to penetrate.

Mr Kim Suk Woo, a senior official at the Economic Planning Board, says that Korea needs closer economic ties with Europe to offset its dependence on the US and Japan. Korean companies are particularly keen, he says, on mergers and joint ventures with European groups since greenfield ventures may not be welcome in the crowded European market. "We complement each other. The Europeans have technology. We have production skills."

The most pressing need is to move offshore operations which have been made uncompetitive by a 100 per cent increase in costs in US dollar terms since 1986, taking account of pay increases and currency appreciation. Labour-intensive industries,

including textiles and electronic assembly work, are establishing new plants in low-wage south-east Asian countries, including Thailand and Indonesia, and in China.

Some 27 per cent of total overseas investment is in the region, much of it in low-capitalised enterprises employing a few hundred people. Samsung assembles video recorders in Thailand, refrigerators in Indonesia and microwaves in Malaysia. Goldstar has consumer appliance factories in Thailand and in Indonesia.

Koreans have already been overseas long enough to experience serious problems. Samsung and Goldstar started their US operations in New Jersey and Alabama respectively by assembling television sets from parts sent from Korea. But the high cost of local labour has driven both companies to switch mainstream television assembly to low-cost Mexico. The American factories now concentrate on large screen televisions and other consumer goods.

"Our expansion has not been totally successful," says Mr Lee of Samsung, "although it has not exactly failed." Korean executives say clashes with local workers have been frequent.

Mr Lee says Koreans have to learn about local culture, which is a polite way of saying that few workers in other countries are prepared to work as hard as Koreans. "If you ask Koreans to work overtime all night to meet an order they'll do it. Whereas in the UK..."

One difficulty is that few Koreans want to work abroad for a long time since such they feel excluded from the mainstream of the company. Another is that no Korean group yet has an integrated group management. The conglomerates are highly decentralised, so knowledge about foreign ventures is not shared easily.

Mr Suh Jung Sun, executive director of Daewoo Capital Management, an arm of the Daewoo conglomerate, says: "Our conclusion for the Daewoo group is that if there were no political pressures from the US and Europe it would definitely be better to produce in South Korea. The same is true for Japan."

THE brash and ambitious Hyundai Group is preparing the third leg of its extraordinary assault on the North American car market.

It has begun selling an attractive updated Excel and has also introduced a more powerful six-cylinder version of its Sonata mid-size model. It has begun production at a new C\$400m (221.8m) assembly plant near Montreal.

The Hyundai Motor Company subsidiary has tried to do in five years what the more cautious Japanese have done in 20. It entered the Canadian market in 1984 with the rear-wheel drive Pony sub-compact and the Stellar compact. In 1985 Hyundai sold almost 80,000 units, mostly in eastern Canada, and built up a dealer network.

In that year it held number one foreign import spot in the Canadian market, well ahead of Toyota, Nissan and Honda. But from that point on it was downhill as buyers found that the Pony could not withstand heavy Canadian usage and the vicious inroads of road salt during winter.

But Canada was the spearhead for the attack on North America, and in that initial thrust Hyundai briefly claimed 21 per cent of the Canadian small car market. It spent C\$8m on advertising alone in 1984-85.

Next, Hyundai Motor, minority owned by Japan's Mitsubishi Corp, launched its second car, the Excel sub-compact, clearly influenced by Mitsubishi and a more rugged model with front-wheel drive.

The Excel shored up Hyundai in Canada, while making one of the most successful imported car introductions ever in the US. More than 250,000 Excels were sold annually in the US in 1986 and 1987, until the novelty wore off and a slow decline set in with tougher competition from the Japanese.

But Hyundai, based on the early Pony success and its confidence in future models, was determined to assemble in Canada for the whole North American market. The C\$400m project astounded the industry with its location at Bromont, near Montreal and C\$10m in Quebec and federal government aid.

Quebec had only one car assembly plant, a General Motors Canada unit, and the political conditions were favourable when Hyundai made its announcement late in 1985.

It was the personal decision of Mr S.Y. Chung, former president of Hyundai Motor. He called in Montreal engineers to design the plant with his company. It was located in a French-speaking area where a young work force could be recruited but the language difficulties have been great.

The plant started commercial production of the Sonata this spring, only a few months behind schedule, and Hyundai is building a C\$120m stamping plant alongside.

Hyundai could not have got that government assistance today. With the 1988 Canada-US Free Trade Pact, Canada has agreed to reduce subsidies for new industrial projects to almost zero. This means continuing support to training programmes, though individual provinces can pay for infrastructure and may offer loan guarantees.

In the first 10 months of 1989 Hyundai sold 24,480 Excels and Sonatas in Canada and 160,700 (mostly Excels) in the US. The comparable figures for 1988 were 26,520 in Canada and 225,000 in the US (all Excels).

The Bromont plant will make between 10,000 and 12,000 Sonatas this year, using a single shift, while the company brings in the higher powered version from Korea with the new more competitive Excel. The Sonatas will also go to Taiwan next year.

In 1991 Bromont will begin making a slightly different Sonata for Chrysler Corporation for delivery in the US. It will only reach the maximum 100,000 units a year by 1991 or 1992 with two shifts.

The Canadian value added is now about 25 per cent, but it will be some time before this reaches the target 50 per cent for maximum tariff advantage on US exports. By 1991, with the Japanese transplants fully in operation, North America expects to have surplus car assembly capacity of 2m units a year. More older assembly plants will have to be closed.

Mr Lee Yoo-II, president of Hyundai Auto Canada Inc, insists the Bromont plant was built to penetrate the North American market which can easily absorb 100,000 Sonatas a year. "We'll market the new Sonata wherever the public demand may be, from Bromont or from Ulsan."

Robert Gibbens

## Hyundai in Canada

## Springboard for a wider assault

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**SOUTH KOREA: FINANCE & INDUSTRY 7**

**LOTTE WORLD**

**Cash rich Koreans help leisure group tap a lucrative market**

THE largest foreign investment in South Korea, is not a semiconductor plant or a car factory, but, perhaps surprisingly, an amusement park. Even more surprisingly for a foreign investment, it is owned by a Korean.

The Lotte World, a giant complex in Seoul includes a Disneyland style fairland and funfair for young and old, a Korean museum and traditional village, a large ice skating rink and an outdoor children's park.

It was established this year by the Lotte Group, a South Korean company whose owner Mr Shin Kyuk Ho, divides his time between Seoul and Tokyo, where he is technically resident and also owns a large company.

The group had sales last year of \$2.5bn in South Korea. Lotte's investments, mainly in hotels, processed food and the amusement park, amount to \$1.7bn, a quarter of the total foreign investment in South Korea over the past 25 years.

"Lotte Shopping" has now become a byword in South Korea for the consumer boom which has swept the country since the Olympic Games were held in Seoul a year ago.

Along with other department

stores the company has seen sales shoot up, as housewives clamour to spend the money which symbolises the country's new prosperity.

Wage disputes and strikes, which have broken out as the country moves from authoritarianism to democracy, have put further cash into people's pockets leading to average monthly income per person of 227bn won has already been achieved. Next year's target is 390bn won and the complex is expected to break even in three years.

The cleverly laid out amusement park was designed by an American company, so lacks the rather grandiose style of the Lotte hotels. Visitors to the complex praised it highly, especially for its ability to cater to

attracts both tourists and Koreans who are nostalgic for tradition, the history of the country is laid out with artistic replicas and includes a look at both ancient court ritual and the lives of ordinary people.

One of the most interesting displays covers the period of the Japanese occupation of Korea, an era which is normally ignored in most government museums, and which might be especially sensitive to a Korean with Japanese interests.

But Mr Shin Kyuk Ho, owner of the group and one of the richest men in Asia, believes that Korea should be honest about its history, and the company has yet to be criticised about the section.

The Lotte group has been one of the first companies to realise the potential of the South Korean market, where local incomes are now the second highest in Asia after Japan and the population is extremely youthful.

Its amusement complex has been so successful that its potential is thought to be broader. In true Korean style Lotte is now working on plans to export the idea to the US.

**'Lotte Shopping' has become a byword for the consumer boom which has recently swept the country. The Lotte group has seen sales shoot up, as housewives clamour to spend the money which symbolises South Korea's new prosperity**

\$652, with Seoul residents earning more than double.

A sense of pride in the country's achievement has also encouraged South Koreans not to worry so much about the cost of the goods they want to buy and to start enjoying their leisure time.

The Lotte World, along with its adjacent hotel and shopping complex, opened partially in January this year and has a sales target of 282bn won (\$420m) for the year, of which

all ages, including very young children.

Although rides and admission fees are rather high, the complex offers Koreans, who have not been able to travel abroad until recently, an international touch, with a French village, an Arabian Nights section and quarters with English and German themes, complete with security guards dressed in the relevant national police costumes.

At the Korean village, which

Maggie Ford

**Valeo-Pyeong Hwa**

**Marriage of foreign expertise and strong domestic demand**

TAEGU, an industrial sprawl on the east of the Korean Peninsula and the country's third largest city, is a world apart from the Paris base of Valeo, one of Europe's largest automotive components manufacturers.

But Valeo has a strategy of establishing design and production centres near the world's largest automobile manufacturers, and nowadays this means Korea. Hence the decision to link up with Pyeong Hwa, one of Korea's two largest clutch makers, and form a joint venture.

"That is the one simple reason why we are here," says Mr Arnaud Le Bec, executive vice-president of Valeo-Pyeong Hwa. "We want to supply car makers like Hyundai, Daewoo and Kia as the Korean automobile industry expands."

Valeo is not alone. Most of the world's large components groups are already in Korea, and this year the automotive sector has been by far the most attractive for foreign companies. In the first nine months, direct investment into the sector totalled \$1.6bn, an increase of more than 200 per cent over the comparable period.

More broadly, Valeo's move illustrates the developing trend of matching foreign interest in

the Korean market with a demand for technology on the part of Korean companies.

If Valeo's incentive motives for setting up the joint venture were clear so too was its choice of partner. Pyeong Hwa clutch, which was built up by Mr Sang Yeong Kim, now the president of the joint venture, supplies all of the clutch requirements of Hyundai Motor Corporation, the country's largest car maker.

Since its expansion into

which has created a company capitalised at \$30m, is on a 50/50 basis. According to Mr Le Bec, this reflects the contributions from both sides.

Valeo supplies technology in two principal ways. Certain equipment which is specific to the company's production process is supplied to the joint venture and then reproduced. The most striking example is a Valeo heat processing machine, alongside which stand three replicas in an early

**Many components groups are already in Korea and this year the automotive sector has been by far the most attractive for foreign companies**

international markets, EMC has been encouraging its suppliers to forge links with US and European companies to improve quality and to develop its own independence from Mitsubishi of Japan, which holds a 15 per cent stake in EMC and which has thus far supplied most of its design and technology requirements. As a result, Pyeong Hwa sought an alliance from among the ranks of the leading international components groups.

The tie-up between Valeo and Pyeong Hwa, which was completed in May 1988 and

stage of development.

Design know-how, in contrast, is imparted by the five expatriate engineers and the establishment of a training course in France for Korean employees.

In return, Valeo receives a share in the valuable Hyundai contract plus additional contracts from Kia and Daewoo, two other local car makers. Combined, these are expected to bring sales of about \$30m next year. Production is based at a new site, opened in January, which is expected to put out more than 2m clutches

next year.

Perhaps more important, the link with EMC provides a strong base through which to develop in the Korean market.

Although the joint venture currently produces only clutches and facings, the longer term aim is to supply other of Valeo's products such as radiators and headlights.

But, for Valeo, the establishment of a potentially lucrative base in the Korean market has not been without difficulties. The negotiations took eight months to complete, partly reflecting differing opinions over whether the contract should include Pyeong Hwa's existing business. Even after signing many obstacles remained.

"Signing the agreement does not mean you are joined," says Mr Le Bec. "The day after you sign you start negotiating again."

One of the principal unresolved areas concerned Valeo's role in day-to-day management and Pyeong Hwa's different management techniques.

The language barrier and the reluctance of the existing management team to relax control meant that Valeo was one step removed from the running of the business. "At the beginning we were like six auditors," notes Mr Le Bec. "The situation has improved day by day, but it is a long process."

In an ideal world he believes that expatriates should spend a year with their prospective joint venture partners to gain experience of the company, its people and how it works. "In the end our contract was a good agreement, well done. But the best lawyers on earth will never solve some of the difficulties which arise."

For a company like Valeo, there is also the question of how to protect its technology and know how. Mr Le Bec believes that the problem is solved by the terms of the joint venture agreement which stipulate that if either company makes clutches elsewhere in Korea it becomes subject to a penalty in excess of \$1m.

Potential problems are also raised by the broader economic environment which this year has seen labour disputes, sharply higher wages and a slowdown in output growth.

Valeo-Pyeong Hwa was one of the few HMC suppliers that did not suffer strikes. Mr Le Bec puts this down to the existing management which retains a relatively firm control over the workforce. He sees this as an important reason for investing in Korea through a joint venture. "As foreigners, last year we could not have controlled the company."

None the less, part of the price for industrial peace was a sharp increase in wages which saw workers' salaries rise by 37 per cent. Since labour costs still account for only 14 per cent of the total this is not too great a concern but the coming spring wage round is seen as critical in determining whether a pattern has been established.

But for Valeo, like many of the foreign investors now coming into Korea, costs are not the central issue. "We are not in Korea to make cheap products," says Mr Le Bec. "We are here because we want to be part of the industry's growth."

John Ridding

**John Ridding on the financial community's ventures overseas**

**Still at an experimental stage**

OVER the past few years, South Korean stockbrokers and life insurance companies have been springing up throughout the world's financial centres.

The handful of the larger securities companies all now have offices in Tokyo, New York, London and Hong Kong, a pattern which is being followed by their smaller counterparts. Life insurance companies too are busily expanding their international departments although so far only the largest, Samsung Life, has representation to match that of the securities houses.

The expansion overseas follows a relaxation in official regulations as part of the government's financial liberalisation strategy.

Last year, certain financial institutions were allowed to make limited overseas investments and will be allowed to open branch offices in 1991. By the following year there should have been a substantial relaxation on the overseas investment permits permitted for individuals and companies as well as for financial institutions.

For the moment the latter may make only small invest-

ments in overseas markets. Securities companies are limited to a total of \$30m while life insurance companies and unit trust companies are limited to \$10m each.

Even within these restricted amounts Korea's institutions have displayed a cautious approach to overseas investment and their total portfolios are well short of the limits. "We are still at the experimental stage," says Mr Roh Tae Ho, manager of overseas investment at Daewoo, the largest securities company.

None the less, the overseas investments do form a pattern. The most favoured stock market has been Tokyo, with London and New York being regarded as relatively unattractive. Most houses have also put a high proportion of their funds into Korean Euro issues, partly to raise short-term profits but with the additional aim of becoming market makers in these instruments.

In the longer term, the international business of Korean financial groups is certain to be a more substantial affair.

The high domestic savings rate and favourable trade balance will continue to create

high liquidity, a proportion of which will flow overseas. Even a small portion of Samsung Life's massive \$10bn of assets would represent a significant increase in outward portfolio investment. In addition, the opening of Korea's own financial markets will provide the opportunity of selling Korean shares to foreigners.

For Mr Ho C Yang, managing director of Dongsuh Securities, the best strategy in international expansion is to be selective. "For the time being we have to find niches and concentrate on activities that we know."

In practice this is likely to mean greater involvement with Korean companies as they expand overseas and look to the Euromarkets for cheap funds. Korean Securities houses have already been active in a number of convertible bond issues, getting their names on tombstones for publicity but also to gain experience of share placings.

Other areas of interest concerning the sale of foreign government bonds to Korean investors are the development of real estate businesses. Samsung Life has already set up a

real estate subsidiary in the US.

But in the development of their international business, Korean institutions will face two principal obstacles. Most immediately there is the problem of gaining expertise in the various foreign markets. This is exacerbated by the traditional insularity of Korea's financial markets and the different dynamics of the Korean stock market. In particular, there is less emphasis on company fundamentals, and like Japan, more official guidance through the large brokers.

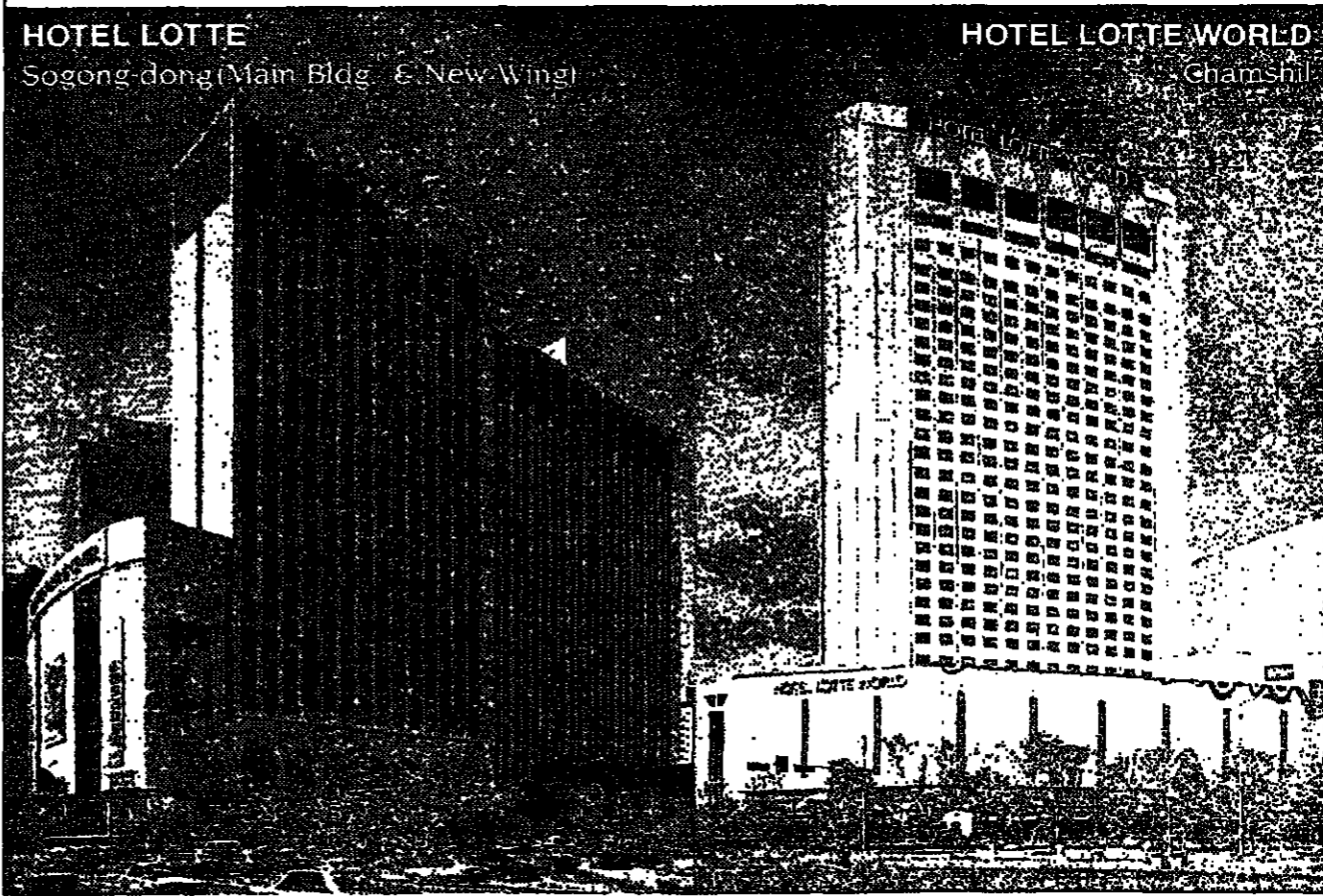
Liberalisation will also bring the domestic institutions into competition with their foreign counterparts. In the domestic market they hold advantages relating to experience and corporate contacts. In addition, they all have large staffs. Daewoo, for example has between 40 and 50 analysts and a dozen economists.

Overseas, however, the Korean institutions are likely to find the going much tougher. Many may feel that the sizeable investments required are too high, particularly when the domestic market offers potentially rapid growth.



Opening up: trading floor of the Korean stock exchange. The Government has set a date of 1992 for liberalising the markets

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